

AUDITING PROCEDURES REPORT

Issued under P.A. 2 of 1968, as amended. Filing is mandatory.

Local Government Type <input checked="" type="checkbox"/> City <input type="checkbox"/> Township <input type="checkbox"/> Village <input type="checkbox"/> Other		Local Government Name City of Cheboygan	County Cheboygan
Audit Date June 30, 2004	Opinion Date August 27, 2004	Date Accountant Report Submitted to State: November 19, 2004	

We have audited the financial statements of this local unit of government and rendered an opinion on financial statements prepared in accordance with the Statements of the **Governmental Accounting Standards Board (GASB)** and the Uniform **Reporting Format** for Financial Statements for Counties and Local **Units of Government** in Michigan by the Michigan Department of Treasury.

We affirm that:

1. We have complied with the *Bulletin for the Audits of Local Units of Government* in Michigan as revised.
2. We are certified public accountants registered to practice in Michigan.

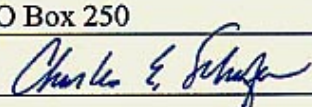
We further affirm the following. "Yes" responses have been disclosed in the financial statements, including the notes, or in the report of comments and recommendations

You must check the applicable box for each item below.

- ☐ yes ☒ no 1. Certain component units/funds/agencies of the local unit are excluded from the financial statements.
- ☐ yes ☒ no 2. There are accumulated deficits in one or more of this unit's unreserved fund balances/retained earnings (P.A. 275 of 1980).
- ☐ yes ☒ no 3. There are instances of non-compliance with the Uniform Accounting and Budgeting Act (P.A. 2 of 1968, as amended).
- ☐ yes ☒ no 4. The local unit has violated the conditions of either an order issued under the Municipal Finance Act or its requirements, or an order issued under the Emergency Municipal Loan Act.
- ☐ yes ☒ no 5. The local unit holds deposits/investments which do not comply with statutory requirements. (P.A. 20 of 1943, as amended [MCL 129.91], or P.A. 55 of 1982, as amended [MCL 38.1132]).
- ☐ yes ☒ no 6. The local unit has been delinquent in distributing tax revenues that were collected for another taxing unit.
- ☐ yes ☒ no 7. The local unit has violated the Constitutional requirement (Article 9, Section 24) to fund current year earned pension benefits (normal costs) in the current year. If the plan is more than 100% funded and the overfunding credits are more than the normal cost requirement, no contributions are due (paid during the year).
- ☐ yes ☒ no 8. The local unit uses credit cards and has not adopted an applicable policy as required by P.A. 266 of 1995 (MCL 129.241).
- ☐ yes ☒ no 9. The local unit has not adopted an investment policy as required by P.A. 196 of 1997 (MCL 129.95).

We have enclosed the following:

	Enclosed	To Be Forwarded	Not Required
The letter of comments and recommendations.	X		
Reports on individual federal financial assistance programs (program audits).			X
Single Audit Reports (ASLGU).			X

Certified Public Accountant (Firm Name) Rehmann Robson		Charles E. Schafer, CPA	
Street Address 902 S. Huron St., PO Box 250	City Cheboygan	State MI	ZIP 49721
Accountant Signature 			

CITY OF CHEBOYGAN
CHEBOYGAN, MICHIGAN



FINANCIAL STATEMENTS

JUNE 30, 2004

CITY OF CHEBOYGAN

TABLE OF CONTENTS

	<u>PAGE</u>
Independent Auditors' Report	1-2
Management's Discussion and Analysis	I -VIII
Basic Financial Statements	
Government-wide Financial Statements	
Statement of Net Assets	3
Statement of Activities	4-5
Fund Financial Statements	
Balance Sheet – Governmental Funds	6-7
Statement of Revenues, Expenditures and Changes in Fund	
Balances – Governmental Funds	8-9
Statement of Revenues, Expenditures and Changes in Fund Balance –	
Budget and Actual	
General Fund	10
Major Street Fund	11
Statement of Net Assets – Proprietary Funds	12
Statement of Revenues, Expenses and	
Changes in Net Assets – Proprietary Funds	13
Statement of Cash Flows – Proprietary Funds	14-15
Statement of Fiduciary Net Assets – Fiduciary Funds	16
Notes to Financial Statements	17-38

CITY OF CHEBOYGAN

TABLE OF CONTENTS

	<u>PAGE</u>
Supplementary Information	
Detail Schedule of Revenues – Budget and Actual – General Fund	39
Detail Schedule of Expenditures and Other Financing Uses – Budget and Actual – General Fund	40
Combining Balance Sheet – Nonmajor Governmental Funds	41
Combining Statement of Revenues, Expenditures and Changes in Fund Balances – Nonmajor Governmental Funds	42
Combining Balance Sheet – Nonmajor Special Revenue Funds	43
Combining Statement of Revenues, Expenditures and Changes in Fund Balances – Nonmajor Special Revenue Funds	44
Combining Balance Sheet – Nonmajor Debt Service Funds	45
Combining Statement of Revenues, Expenditures and Changes in Fund Balances – Nonmajor Debt Service Funds	46
Combining Balance Sheet – Nonmajor Capital Project Funds	47
Combining Statement of Revenues, Expenditures and Changes in Fund Balances – Nonmajor Capital Project Funds	48
Combining Statement of Changes in Assets and Liabilities – All Agency Funds	49
Balance Sheet and Statement of Net Assets – Component Unit	50
Statement of Revenues, Expenditures and Changes in Fund Balance and Statement of Activities – Component Unit	51
 Internal Control and Compliance	
Independent Auditors’ Report on Compliance and on Internal Control Over Financial Reporting Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards	52-53



INDEPENDENT AUDITORS' REPORT

August 27, 2004

Honorable Mayor and Members
of the City Council
City of Cheboygan
Cheboygan, Michigan

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the discretely presented component unit, each major fund, and the aggregate remaining fund information of the **City of Cheboygan**, (the "City"), as of and for the year ended June 30, 2004, which collectively comprise the City's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the City's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, the discretely presented component unit, each major fund, and the aggregate remaining fund information of the City, as of June 30, 2004, and the respective changes in financial position and cash flows, where applicable, thereof and the respective budgetary comparisons for each major fund for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis on pages I through VIII is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

As described on Note H, the City adopted the provisions of Governmental Accounting Standards Board Statement No.'s 34, 37 and 38 and GASB Interpretation 6 as of and for the year ended June 30, 2003. This results in a change in the City's format and content of the basic financial statements.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City's basic financial statements. The supplementary information listed in the table of contents is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly presented in all material respects in relation to the basic financial statements taken as a whole.

In accordance with *Government Auditing Standards*, we have also issued our report dated August 27, 2004, on our consideration of the City's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

A handwritten signature in black ink, reading "Lehmann Johnson". The signature is written in a cursive, flowing style with a large initial 'L'.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Management's Discussion and Analysis

As management of the **City of Cheboygan, Michigan** (the "City"), we offer readers of the City's financial statements this narrative overview and analysis of the financial activities of the City for the fiscal year ended June 30, 2004. We encourage readers to consider the information presented here in conjunction with additional information that is furnished in the financial statements and notes to the financial statements.

Financial Highlights

- The assets of the City exceeded its liabilities at the close of fiscal year 2004 by \$14,261,160 (*net assets*). Of this \$1,905,985 (*unrestricted net assets*) may be used to meet the City's ongoing obligations to citizens and creditors.
- The restatements of the fund balances are necessary due to the implementation of GASB Statement No. 34. Comparative data is not presented because of the conversion to GASB Statement No. 34 during the current year.
- The voters of the City passed a bond proposal in the amount of \$1,350,000 for an addition to the Department of Public Safety building. Among the improvements will be an interrogation room, showers, additional office and conference space, and in-door parking for police and fire vehicles.
- The City has also created funds to cover the future cost of retiree Blue Cross and the payment of sick and vacation time accruals at the time of retirement. As of June 30, 2004, the fund balances were \$212,455 and \$119,378, respectively.
- At the end of the current fiscal year, unreserved fund balance for the General Fund was \$875,676 or 40% of the total General Fund expenditures and transfers.

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the City's basic financial statements. The City's basic financial statements comprise three components: 1) government-wide financial statements, 2) fund financial statements and 3) notes to the financial statements. This report also contains other supplementary information in addition to the financial statements themselves.

Government-wide financial statements. The *government-wide financial statements* are designed to provide readers with a broad overview of the City's finances, in a manner similar to a private-sector business.

The *statement of net assets* presents information on all of the City's assets and liabilities, with the difference between the two reported as *net assets*. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the City is improving or deteriorating.

The *statement of activities* presents information showing how the government's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods (e.g., earned but unused vacation leave and accrued interest expense).

Both of the government-wide financial statements distinguish functions of the City that are principally supported by taxes and intergovernmental revenues (*governmental activities*) from other functions that are intended to recover all or a significant portion of their costs through user fees and charges (*business-type activities*). The governmental activities of the City include legislative, general government, public safety, public works and culture and recreation. The business-type activities include the sewer and water activities.

The government-wide financial statements include not only the City itself (known as the *primary government*), but also the Cheboygan Downtown Development Authority, a legally separate component unit for which the City is financially accountable.

The government-wide financial statements can be found on pages 3-5 of this report.

Fund financial statements. A *fund* is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The City, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the City can be divided into three categories: governmental funds, proprietary funds, and fiduciary funds.

Governmental funds. *Governmental funds* are used to account for essentially the same functions reported as *governmental activities* in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on *near-term inflows and outflows of spendable resources*, as well as on *balances of spendable resources* available at the end of the fiscal year. Such information may be useful in evaluating a government's near-term financing requirements.

Because the focus of *governmental funds* is narrower than that of the government-wide financial statements, it is useful to compare the information presented for *governmental funds* with similar information presented for *governmental activities* in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between *governmental funds* and *governmental activities*.

The City maintains 23 individual governmental funds. Information is presented separately in the governmental fund balance sheet and in the governmental fund statement of revenues, expenditures, and changes in fund balances for the General Fund, Major Street Fund, 2001 Sidewalk Special Assessment Bond Fund, 2000 Streetscape Special Assessment Bond Fund and 2004 General Obligation Bond Construction Fund, each of which are considered to be major funds. Data from the other 18 governmental funds are combined into a single, aggregated presentation. Individual fund data for each of these nonmajor governmental funds is provided in the form of combining statements elsewhere in this report.

The City adopts an annual appropriated budget for its General and Special Revenue Funds. Budgetary comparison statements have been provided herein to demonstrate compliance with the General Fund and the major Special Revenue Fund.

The basic *governmental fund* financial statements can be found on pages 6-11 of this report.

Proprietary funds. The City maintains two different types of proprietary funds. *Enterprise Funds* are used to report the same functions presented as *business-type activities* in the government-wide financial statements. The City uses Enterprise Funds to account for its water and sewer operations. *Internal Service Funds* are an accounting device used to accumulate and allocate costs internally among the various City functions. The City of Cheboygan uses its Internal Service Fund to account for its motor pool activities.

Proprietary funds provide the same type of information as the government-wide financial statements, only in more detail. The proprietary fund financial statements provide separate information for the Water and Sewer departments which are considered major enterprise funds of the City.

The basic proprietary fund financial statements can be found on 12-15 of this report.

Fiduciary funds. Fiduciary funds are used to account for resources held for the benefit of parties outside the government. Fiduciary funds are not reflected in the government-wide financial statements because the resources of those funds are not available to support the City's own programs. The accounting used for fiduciary funds is much like that used for governmental funds.

The basic fiduciary fund financial statements can be found on page 16 of this report.

Notes to the financial statements. The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements can be found on pages 17-38 of this report.

Other information. In addition to the basic financial statements and accompanying notes, this report also presents certain *supplementary information* including the combining statements referred to earlier in connection with nonmajor governmental and fiduciary funds which are presented immediately following the notes to the financial statements. Combining and individual fund statements and schedules can be found on pages 39-51 of this report.

Government-wide Financial Analysis

Net assets may serve over time as a useful indicator of a government's financial position. In the case of the City, assets exceeded liabilities by \$14,261,160 at the close of fiscal year 2004.

Approximately 74% of the City's net assets reflects its investment in net capital assets (e.g., land, buildings, vehicles and equipment); less any related debt used to acquire those assets that is still outstanding. The City uses these capital assets to provide services to citizens; consequently, these assets are *not* available for future spending. Although the City's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from

other sources, since the capital assets themselves cannot be used to liquidate these liabilities. Net assets restricted for debt service, capital projects and perpetual care represent approximately 9% of total net assets. The remaining balance of *unrestricted net assets* (\$1,905,985) may be used to meet the government's ongoing obligation to citizens and creditors.

Because this is the first year of implementation of Government Accounting Standards Board Statement No. 34, which requires this new reporting model, the following tables present only current year data. In future years, when prior year information is available, comparative analysis of government-wide data will be presented.

**City of Cheboygan
Net Assets**

	<u>Governmental Activities</u>	<u>Business-Type Activities</u>	<u>Total</u>
Assets			
Cash and other assets	\$ 3,293,940	\$ 886,200	\$ 4,180,140
Capital assets, net of accumulated depreciation, where applicable	<u>7,798,547</u>	<u>10,131,988</u>	<u>17,930,535</u>
Total assets	<u>11,092,487</u>	<u>11,018,188</u>	<u>22,110,675</u>
Liabilities			
Current and other liabilities	660,539	41,093	701,632
Long-term debt, net of current portion	<u>7,147,883</u>	<u>-</u>	<u>7,147,883</u>
Total liabilities	<u>7,808,422</u>	<u>41,093</u>	<u>7,849,515</u>
Net assets			
Invested in capital assets, net of related debt	412,170	10,131,988	10,544,158
Restricted for debt service, capital projects and perpetual care	1,811,017	-	1,811,017
Unrestricted	<u>1,060,878</u>	<u>845,107</u>	<u>1,905,985</u>
Total net assets	<u>\$ 3,284,064</u>	<u>\$ 10,977,095</u>	<u>\$ 14,261,160</u>

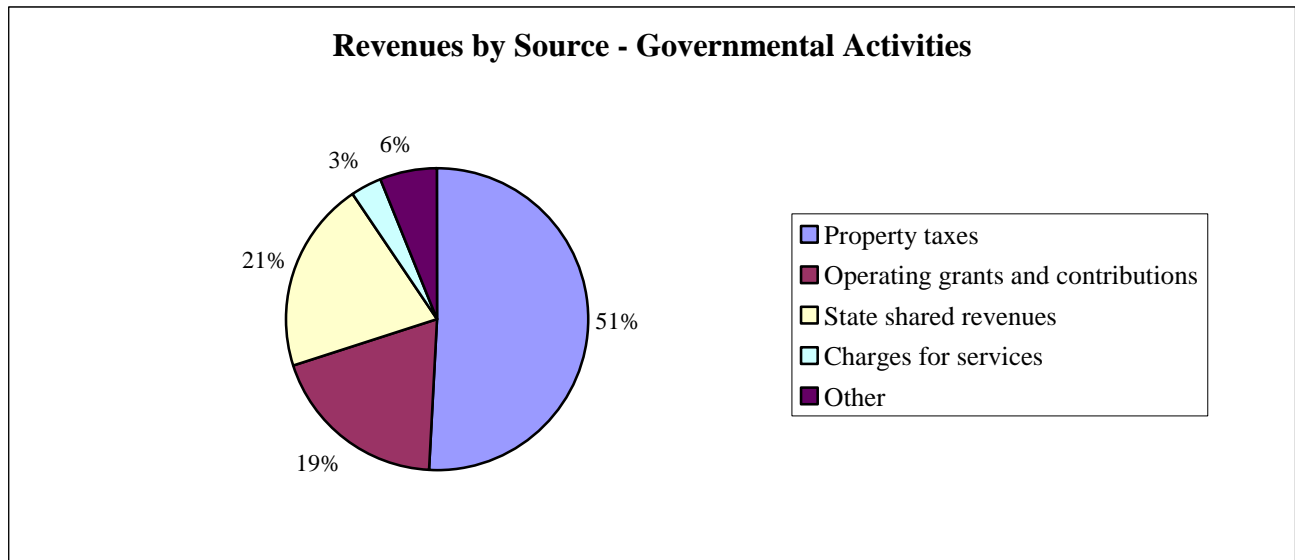
At the end of the current fiscal year, the City is able to report positive balances in all three categories of net assets, for the government as a whole and for its separate governmental and business-type activities.

The City's net assets increased \$66,319 during the current fiscal year.

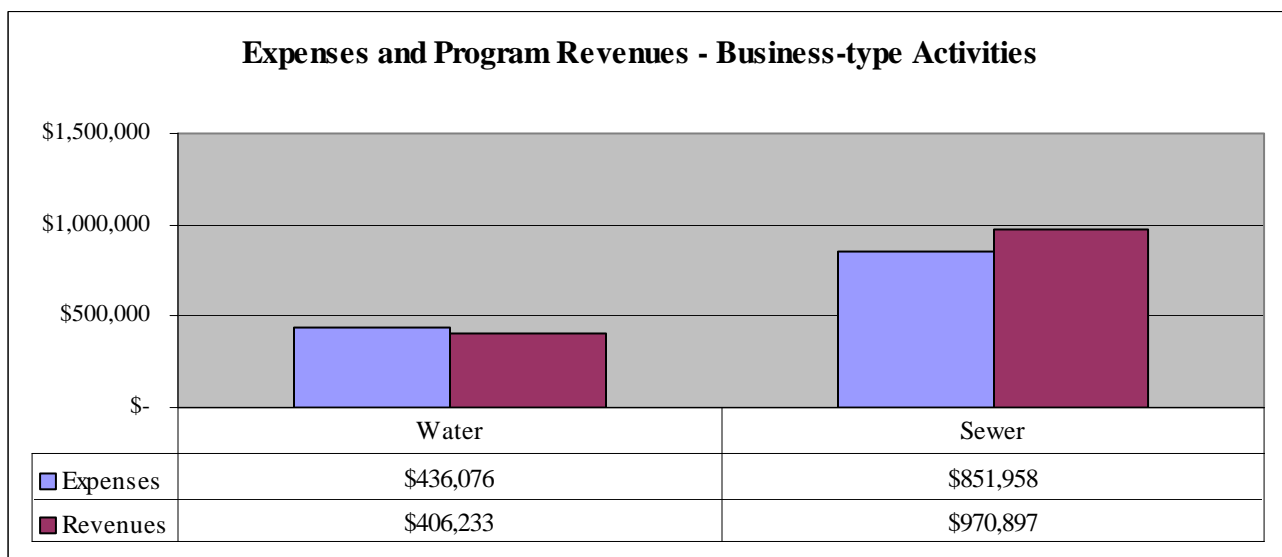
City of Cheboygan
Changes in Net Assets

	Governmental	Business-Type	
	<u>Activities</u>	<u>Activities</u>	<u>Total</u>
Revenues			
Program revenues			
Charges for services	\$ 105,809	\$ 1,341,183	\$ 1,446,992
Operating grants and contributions	618,601	35,947	654,548
General revenues			
Property taxes – general operating	1,321,744	-	1,321,744
Property taxes – debt	314,275	-	314,275
State shared revenues	668,575	-	668,575
Gain of sale of capital assets	6,105	-	6,105
Interest earnings	27,072	4,933	32,005
Transfers-internal activities	27,625	(27,625)	-
Transfers-component unit	<u>131,400</u>	<u>-</u>	<u>131,400</u>
Total revenues	<u>3,221,206</u>	<u>1,354,438</u>	<u>4,575,644</u>
Expenses			
Legislative	46,575	-	46,575
General government	731,494	-	731,494
Public safety	884,706	-	884,706
Public works	962,030	-	962,030
Culture and recreation	301,293	-	301,293
Sewer	-	851,958	851,958
Water	-	436,076	436,076
Interest on long-term debt	<u>295,193</u>	<u>-</u>	<u>295,193</u>
Total expenses	<u>3,221,291</u>	<u>1,288,034</u>	<u>4,509,325</u>
Change in net assets	(85)	66,404	66,319
Net assets - beginning of year, as restated	<u>3,284,150</u>	<u>10,910,691</u>	<u>14,194,841</u>
Net assets - end of year	<u>\$ 3,284,065</u>	<u>\$ 10,977,095</u>	<u>\$ 14,261,160</u>

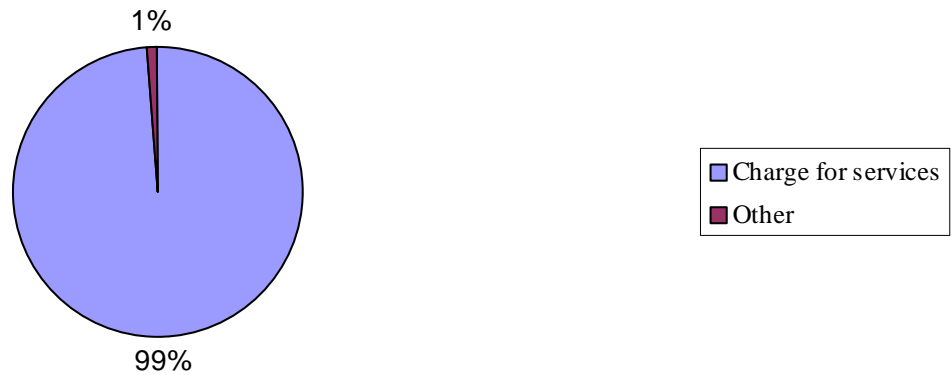
Governmental activities. Governmental activities decreased the City's net assets by \$85.



Business-type activities. Business-type activities increased the City's net assets by \$66,404, accounting for substantially all of the total increase in the City's net assets for fiscal year 2004.



Revenues by Source - Business-type Activities



Financial Analysis of the Government's Funds

As noted earlier, the City uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

Governmental funds. The focus of the City's *governmental funds* is to provide information on near-term inflows, outflows, and balances of *spendable* resources. Such information is useful in assessing the City's financing requirements. In particular, *unreserved fund balance* may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year.

The General Fund is the main operating fund of the City. General Fund fund balance decreased by \$14,426 from \$890,102 to \$875,676 during 2004.

Proprietary funds. The City *proprietary fund statements* provide the same type of information found in the government-wide financial statements, but in more detail.

General Fund Budgetary Highlights

The City's budget was amended due to a federal grant that was awarded the City; however, the project was not started prior to the current fiscal year end . That being said, the remaining revenue budget increased due to higher than expected state revenues and property taxes. The expense budget was amended due to the grant project that was not undertaken during the fiscal year.

Capital Asset and Debt Administration

Capital assets – The City defines a capital asset as an asset whose cost exceeds \$5,000 and whose useful life is greater than two years. Included in the cost of a capital asset are items such as labor and freight and any other costs associated with bringing the asset into full operation. Assets are depreciated using the straight-line method over the course of their useful lives.

City of Cheboygan
Capital Assets
(net of depreciation, where applicable)

	Governmental	Business-type	
	<u>Activities</u>	<u>Activities</u>	<u>Total</u>
Land	\$ 200,000	\$ 2,251	\$ 202,251
Buildings and improvements	3,179,757	814,256	3,994,013
Land improvements	1,892,048	-	1,892,048
Machinery and equipment	853,377	428,512	1,281,889
Infrastructure	<u>1,673,365</u>	<u>8,886,969</u>	<u>10,560,334</u>
Total	<u>\$ 7,798,547</u>	<u>\$ 10,131,988</u>	<u>\$17,930,535</u>

Additional information on the City's capital assets can be found in Note 3C on pages 25-27 of this report.

Long-term debt. Debt incurred in the course of constructing or acquiring a capital asset is recorded and paid for from a Debt Service Fund or Internal Service Fund. Debt is classified as long-term if the debt matures in a period greater than one year.

The City issued the 2004 General Obligation Construction bonds for \$1,350,000 during the year. The proceeds will be used to construct a new public safety building.

Additional information on the City's long-term debt can be found in Note 3F on pages 28-33 of this report.

Economic Factors and Next Year's Budgets and Rates

The City continues to experience increases in property values, which increases property tax revenues. However, the increased revenues generated from property tax increases have been largely offset by decreases in state shared revenue, due to the State of Michigan's current financial difficulties. The City of Cheboygan continues to review methods for delivery of services and continues to seek grants and other funding sources.

The 2004/2005 budget projects continued growth in taxable property values with state shared revenues remaining at the previous year's levels. Transfers from the City's General Fund will be necessary to continue funding projects, programs, and services as set forth in the City's annual Budget and Capital Improvement Plan. The City of Cheboygan will continue to monitor closely its capital needs, service requirements, and upcoming projects as they relate to budget and projected revenue streams.

Requests for Information

This financial report is designed to provide a general overview of the City's finances for all those with an interest in the City's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the City Treasurer's Office, City of Cheboygan, Michigan, 403 N. Huron St., PO Box 39, Cheboygan, Michigan, 49721.

BASIC FINANCIAL STATEMENTS

GOVERNMENT-WIDE FINANCIAL STATEMENTS

CITY OF CHEBOYGAN
STATEMENT OF NET ASSETS

JUNE 30, 2004

	Primary Government			Component Unit
	Governmental Activities	Business-type Activities	Total	Downtown Development Authority
Assets				
Cash and cash equivalents	\$ 2,699,225	\$ 695,375	\$ 3,394,600	\$ 225,546
Accounts receivable	455,634	190,825	646,459	-
Capital assets, net	7,798,547	10,131,988	17,930,535	150,000
Restricted cash	41,329	-	41,329	-
Restricted investments	97,752	-	97,752	-
Total assets	11,092,487	11,018,188	22,110,675	375,546
Liabilities				
Accounts payable and accrued expenditures	175,103	26,916	202,019	1,077
Customer deposits	-	14,177	14,177	-
Deferred revenue	11,849	-	11,849	-
Noncurrent liabilities				
Due within one year	473,587	-	473,587	13,300
Due in more than one year	7,147,883	-	7,147,883	-
Total liabilities	7,808,422	41,093	7,849,515	14,377
Net assets				
Invested in capital assets, net of related debt	412,170	10,131,988	10,544,158	136,700
Restricted for				
Debt service	337,090	-	337,090	-
Capital projects	1,334,846	-	1,334,846	-
Perpetual care	139,081	-	139,081	-
Unrestricted	1,060,878	845,107	1,905,985	224,469
Total net assets	\$ 3,284,065	\$ 10,977,095	\$ 14,261,160	\$ 361,169

The accompanying notes are an integral part of these financial statements.

CITY OF CHEBOYGAN
STATEMENT OF ACTIVITIES

FOR THE YEAR ENDED JUNE 30, 2004

Functions / Programs	Expenses	Program Revenues			Net (Expense) Revenue
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	
Primary government					
Governmental activities					
Legislative	\$ 46,575	\$ -	\$ -	\$ -	\$ (46,575)
General government	731,494	80,263	60,551	-	(590,680)
Public safety	884,706	19,958	3,340	-	(861,408)
Public works	962,030	3,500	547,310	-	(411,220)
Culture and recreation	301,293	2,088	7,400	-	(291,805)
Interest on long-term debt	295,193	-	-	-	(295,193)
Total governmental activities	3,221,291	105,809	618,601	-	(2,496,881)
Business-type activities					
Sewer	851,958	949,808	21,089	-	118,939
Water	436,076	391,375	14,858	-	(29,843)
Total business-type activities	1,288,034	1,341,183	35,947	-	89,096
Total primary government	\$ 4,509,325	\$ 1,446,992	\$ 654,548	\$ -	\$ (2,407,785)
Component unit					
Downtown Development Authority	\$ 5,309	\$ -	\$ -	\$ -	\$ (5,309)

Continued...

CITY OF CHEBOYGAN
STATEMENT OF ACTIVITIES

FOR THE YEAR ENDED JUNE 30, 2004

	Primary Government			Component Unit
	Governmental	Business-type		Downtown
	Activities	Activities	Total	Development Authority
Changes in net assets				
Net (expense) revenue	\$ (2,496,881)	\$ 89,096	\$ (2,407,785)	\$ (5,309)
General revenues				
Property taxes				
General operating	1,321,744	-	1,321,744	155,342
Debt	314,275	-	314,275	-
State shared revenues	668,575	-	668,575	-
Gain on sale of capital assets	6,105	-	6,105	-
Interest earnings	27,072	4,933	32,005	1,869
Transfers - internal activities	27,625	(27,625)	-	-
Transfers - component unit	131,400	-	131,400	(131,400)
Total general revenues and transfers	2,496,796	(22,692)	2,474,104	25,811
Change in net assets	(85)	66,404	66,319	20,502
Net assets, beginning of year, as restated	3,284,150	10,910,691	14,194,841	340,667
Net assets, end of year	\$ 3,284,065	\$ 10,977,095	\$ 14,261,160	\$ 361,169

Concluded

The accompanying notes are an integral part of these financial statements.

FUND FINANCIAL STATEMENTS

CITY OF CHEBOYGAN

BALANCE SHEET GOVERNMENTAL FUNDS

JUNE 30, 2004

		Special Revenue Fund		Debt Service Funds	
		Major Street	2001 Sidewalk Special Assessment Bond	2000 Streetscape Special Assessment Bond	
ASSETS	General				
Cash and cash equivalents	\$ 849,089	\$ (12,414)	\$ 20,360	\$ 11,943	
Accounts receivable	4,186	-	-	-	
Due from other governmental units	98,110	54,212	-	-	
Special assessments receivable	69,088	-	49,795	156,683	
Restricted cash					
Restricted investments					
Total assets	\$ 1,020,473	\$ 41,798	\$ 70,155	\$ 168,626	
LIABILITIES AND FUND BALANCES					
Liabilities					
Accounts payable	\$ 9,160	\$ 739	\$ -	\$ -	
Accrued expenses	43,075	485	-	-	
Due to other governmental units	11,624	-	-	-	
Deferred revenue	80,938	-	49,795	156,683	
Total liabilities	144,797	1,224	49,795	156,683	
Fund balances					
Reserved					
Termination liability	-	-	-	-	
Retiree BC/BS	-	-	-	-	
Perpetual care					
Debt service	-	-	20,360	11,943	
Capital projects	-	-	-	-	
Unreserved					
Designated for subsequent years expenditures	101,605	-	-	-	
Undesignated, General Fund	774,071	-	-	-	
Undesignated, Special Revenue Funds	-	40,574	-	-	
Total fund balances	875,676	40,574	20,360	11,943	
Total liabilities and fund balances	\$ 1,020,473	\$ 41,798	\$ 70,155	\$ 168,626	

Capital Project Fund		
2004		
General		
Obligation		
Bond	Nonmajor	
Construction	Funds	Total
\$ 1,348,275	\$ 481,972	\$ 2,699,225
-	324	4,510
-	23,236	175,558
-	-	275,566
	41,329	41,329
	97,752	97,752
\$ 1,348,275	\$ 644,613	\$ 3,293,940

\$ 24,845	\$ 4,428	\$ 39,172
-	531	44,091
-	-	11,624
-	-	287,416
24,845	4,959	382,303

-	119,378	119,378
-	212,455	212,455
	139,081	139,081
-	98,309	130,612
1,323,430	11,416	1,334,846
-	-	101,605
-	-	774,071
-	59,015	99,589
1,323,430	639,654	2,911,637
\$ 1,348,275	\$ 644,613	\$ 3,293,940

Continued...

CITY OF CHEBOYGAN

**BALANCE SHEET
GOVERNMENTAL FUNDS**

JUNE 30, 2004

**Reconciliation of fund balances on the balance sheet for governmental activities
to the statement of net assets**

Fund balances - total governmental funds **\$ 2,911,637**

Amounts reported for governmental activities in the statement of net assets are different because

Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds.

Add - capital assets (net) 6,932,411

Certain assets, such as special assessments receivable, are not due and receivable in the current period and therefore are offset with deferred revenue in the funds.

Add - deferred revenue on special assessments receivable 275,566

Internal service funds are used by management to charge the costs of certain activities, such as equipment costs, to individual funds. The assets and liabilities of the internal service fund are included in governmental activities in the statement of net assets.

Add - net assets of governmental activities accounted for in an internal service fund 507,351

Certain liabilities, such as bonds payable, are not due and payable in the current period and therefore are not reported in the funds.

Deduct - compensated absences payable (235,093)

Deduct - bonds payable (7,034,000)

Deduct - accrued interest on bonds payable (73,807)

Net assets of governmental activities **\$ 3,284,065**

Concluded

The accompanying notes are an integral part of these financial statements.

CITY OF CHEBOYGAN
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES
IN FUND BALANCES - GOVERNMENTAL FUNDS
FOR THE YEAR ENDED JUNE 30, 2004

		Special Revenue Fund	Debt Service Funds	
			2001 Sidewalk Special Assessment Bond	2000 Streetscape Special Assessment Bond
	General	Major Street		
Revenues				
Taxes	\$ 1,358,791	\$ -	\$ -	\$ -
Special assessments	-	-	5,790	21,525
Licenses and permits	10,759	-	-	-
Federal revenues	968	-	-	-
State revenues	677,309	390,721	-	-
Charges for services	27,474	-	-	-
Interest	15,217	366	3,521	10,574
Miscellaneous	60,672	-	-	-
Total revenues	2,151,190	391,087	9,311	32,099
Expenditures				
Current				
Legislative	46,575	-	-	-
General government	511,221	-	-	-
Public safety	863,747	-	-	-
Public works	242,182	252,494	-	-
Culture and recreation	239,585	-	-	-
Capital outlay	-	-	-	-
Debt service				
Principal retirement	-	-	3,000	25,000
Interest and fiscal charges	-	-	2,345	8,994
Total expenditures	1,903,310	252,494	5,345	33,994
Revenues over (under) expenditures	247,880	138,593	3,966	(1,895)
Other financing sources (uses)				
Bond proceeds	-	-	-	-
Transfers in	-	-	-	-
Transfers out	(262,306)	(111,984)	-	-
Transfer in from component unit	-	-	-	-
Total other financing (uses)	(262,306)	(111,984)	-	-
Net change in fund balances	(14,426)	26,609	3,966	(1,895)
Fund balance, beginning of year	890,102	13,965	16,394	13,838
Fund balance, end of year	\$ 875,676	\$ 40,574	\$ 20,360	\$ 11,943

Capital Project Fund		
2004		
General		
Obligation		
Bond	Nonmajor	
Construction	Funds	Total
\$ -	\$ 314,275	\$ 1,673,066
-	-	27,315
-	-	10,759
-	-	968
-	156,223	1,224,253
-	14,600	42,074
275	13,486	43,439
-	17,610	78,282
275	516,194	3,100,156
-	-	46,575
-	157,817	669,038
-	-	863,747
-	237,379	732,055
-	-	239,585
26,845	11,051	37,896
-	314,000	342,000
-	283,792	295,131
26,845	1,004,039	3,226,027
(26,570)	(487,845)	(125,871)
1,350,000	-	1,350,000
-	476,989	476,989
-	(71,274)	(445,564)
-	131,400	131,400
1,350,000	537,115	1,512,825
1,323,430	49,270	1,386,954
-	590,384	1,524,683
\$ 1,323,430	\$ 639,654	\$ 2,911,637

Continued...

CITY OF CHEBOYGAN
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES
IN FUND BALANCE - GOVERNMENTAL FUNDS

FOR THE YEAR ENDED JUNE 30, 2004

Reconciliation of the statement of revenues, expenditures and change in fund balance of governmental funds to the statement of activities

Net change in fund balances - total governmental funds	\$ 1,386,954
---	---------------------

Amounts reported for governmental activities in the statement of activities are different because

Governmental funds report capital outlays as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense.

Add - capital outlay	55,287
Deduct - depreciation expense	(340,904)

Special assessments receivable are long-term in nature and are collectable over several years. However, only the current receipts are reflected as revenues on the fund statements.

Deduct - special assessment receipts	(37,975)
--------------------------------------	----------

Bond proceeds provide current financial resources to governmental funds in the period issued, but issuing bonds increases long-term liabilities in the statement of net assets. Repayment of bond principal is an expenditure in the governmental funds, but the repayment reduces long-term liabilities in the statement of net assets.

Add - principal payments on long-term liabilities	342,000
Deduct - bond proceeds	(1,350,000)

Internal service funds are used by management to charge the costs of certain activities, such as equipment costs, to individual funds. The net revenue (expense) of certain internal service funds is reported with governmental activities.

Net loss from governmental activities accounted for in internal service fund	(45,739)
--	----------

Some expenses reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in the funds.

Add - decrease in compensated absences	(9,649)
Deduct - current year increase in accrued interest	(59)

Change in net assets of governmental activities	\$ (85)
--	----------------

Concluded

The accompanying notes are an integral part of these financial statements.

CITY OF CHEBOYGAN
STATEMENT OF REVENUES, EXPENDITURES
AND CHANGES IN FUND BALANCE
BUDGET AND ACTUAL - GENERAL FUND
FOR THE YEAR ENDED JUNE 30, 2004

	Budget		Actual	Variance With Amended Budget Positive (Negative)
	Original	Amended		
Revenues				
Taxes	\$ 1,299,500	\$ 1,353,600	\$ 1,358,791	\$ 5,191
Licenses and permits	8,000	9,000	10,759	1,759
Federal revenues	105,000	-	968	968
State revenues	644,450	676,200	677,309	1,109
Charges for services	52,000	27,400	27,474	74
Interest	13,000	11,000	15,217	4,217
Miscellaneous	50,000	69,600	60,672	(8,928)
Total revenues	2,171,950	2,146,800	2,151,190	4,390
Expenditures				
Legislative	42,000	46,575	46,575	-
General government	515,200	519,900	511,221	8,679
Public safety	852,510	873,500	863,747	9,753
Public works	186,140	242,182	242,182	-
Culture and recreation	417,975	253,025	239,585	13,440
Total expenditures	2,013,825	1,935,182	1,903,310	31,872
Revenues over expenditures	158,125	211,618	247,880	36,262
Other financing sources (uses)				
Transfers out	(349,645)	(265,322)	(262,306)	3,016
Net change in fund balance	(191,520)	(53,704)	(14,426)	39,278
Fund balance, beginning of year	890,102	890,102	890,102	-
Fund balance, end of year	\$ 698,582	\$ 836,398	\$ 875,676	\$ 39,278

The accompanying notes are an integral part of these financial statements.

CITY OF CHEBOYGAN

STATEMENT OF REVENUES, EXPENDITURES
AND CHANGES IN FUND BALANCE
BUDGET AND ACTUAL - MAJOR STREET FUND

FOR THE YEAR ENDED JUNE 30, 2004

	Budget		Actual	Variance With Amended Budget Positive (Negative)
	Original	Amended		
Revenues				
State revenues	\$ 360,000	\$ 376,500	\$ 390,721	\$ 14,221
Interest	-	-	366	366
Total revenues	360,000	376,500	391,087	14,587
Expenditures				
Public works	302,395	264,640	252,494	12,146
Revenues over expenditures	57,605	111,860	138,593	26,733
Other financing uses				
Transfers out	(58,605)	(113,880)	(111,984)	1,896
Net change in fund balance	(1,000)	(2,020)	26,609	28,629
Fund balance, beginning of year	13,965	13,965	13,965	-
Fund balance, end of year	\$ 12,965	\$ 11,945	\$ 40,574	\$ 28,629

The accompanying notes are an integral part of these financial statements.

CITY OF CHEBOYGAN
STATEMENT OF NET ASSETS
PROPRIETARY FUNDS

JUNE 30, 2004

	<u>Sewer</u>	<u>Water</u>	<u>Total</u>	<u>Internal Service Fund</u>
Assets				
Current assets				
Cash and cash equivalents	\$ 582,075	\$ 113,300	\$ 695,375	\$ -
Accounts receivable	131,205	59,620	190,825	-
Total current assets	713,280	172,920	886,200	-
Property and equipment, net of accumulated depreciation	6,559,109	3,572,879	10,131,988	866,136
Total assets	7,272,389	3,745,799	11,018,188	866,136
Liabilities				
Current liabilities				
Accounts payable	12,129	11,892	24,021	5,955
Accrued expenses	1,742	1,153	2,895	453
Customer deposits	-	14,177	14,177	-
Current portion of long term debt	-	-	-	112,093
Total current liabilities	13,871	27,222	41,093	118,501
Noncurrent liabilities				
Notes payable	-	-	-	240,284
Total liabilities	13,871	27,222	41,093	358,785
Net assets				
Investment in capital assets - net of related debt	6,559,109	3,572,879	10,131,988	625,852
Unrestricted (deficit)	699,409	145,698	845,107	(118,501)
Total net assets	\$ 7,258,518	\$ 3,718,577	\$ 10,977,095	\$ 507,351

The accompanying notes are an integral part of these financial statements.

CITY OF CHEBOYGAN

STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS - PROPRIETARY FUNDS

FOR THE YEAR ENDED JUNE 30, 2004

	Sewer	Water	Total	Internal Service Fund
Operating revenues				
Charges for services	\$ 949,808	\$ 391,375	\$ 1,341,183	\$ 362,618
Operating expenditures				
Personal services	275,737	227,336	503,073	65,509
Contracted services	58,137	23,747	81,884	5,706
Insurance	25,022	3,687	28,709	33,023
Equipment rental	33,642	16,108	49,750	348
Supplies	92,274	35,643	127,917	48,271
Utilities	86,298	35,129	121,427	16,531
Repairs and maintenance	200	-	200	49,803
Depreciation	269,993	89,516	359,509	166,620
Miscellaneous	10,655	4,910	15,565	-
Total operating expenses	851,958	436,076	1,288,034	385,811
Operating income (loss)	97,850	(44,701)	53,149	(23,193)
Nonoperating revenues (expenses)				
Interest revenue	4,022	911	4,933	-
Penalties	12,046	6,358	18,404	-
Miscellaneous revenue	9,043	8,500	17,543	-
Interest expense	-	-	-	(18,746)
Total nonoperating revenues (expenses)	25,111	15,769	40,880	(18,746)
Income (loss) before transfers	122,961	(28,932)	94,029	(41,939)
Transfers				
Transfers out	(16,625)	(11,000)	(27,625)	(3,800)
Change in net assets	106,336	(39,932)	66,404	(45,739)
Net assets, beginning of year, as restated	7,152,182	3,758,509	10,910,691	553,090
Net assets, end of year	\$ 7,258,518	\$ 3,718,577	\$ 10,977,095	\$ 507,351

The accompanying notes are an integral part of these financial statements.

CITY OF CHEBOYGAN
STATEMENT OF CASH FLOWS
PROPRIETARY FUNDS

FOR THE YEAR ENDED JUNE 30, 2004

	<u>Sewer</u>	<u>Water</u>	<u>Total</u>	<u>Internal Service Fund</u>
Cash flows from operating activities				
Cash collected from customers	\$ 945,181	\$ 386,624	\$ 1,331,805	\$ -
Cash collected from other funds	-	-	-	362,618
Cash paid for employee wages and benefits	(275,737)	(227,336)	(503,073)	(65,509)
Cash paid for other operating and administrative expenses	(297,408)	(148,452)	(445,860)	(128,239)
Net cash provided by operating activities	372,036	10,836	382,872	168,870
Cash flows from non-capital financing activities				
Transfers out	(16,625)	(11,000)	(27,625)	(3,800)
Penalties	12,046	6,358	18,404	-
Miscellaneous revenue	9,043	8,500	17,543	-
Net cash provided by (used in) non-capital financing activities	4,464	3,858	8,322	(3,800)
Cash flows from capital and related financing activities				
Interest payments	-	-	-	(18,746)
Principal payments	-	-	-	(90,440)
Purchase of property and equipment	(12,179)	(65,619)	(77,798)	(55,884)
Net cash used in capital and related financing activities	(12,179)	(65,619)	(77,798)	(165,070)
Cash flows from investing activities				
Interest revenue	4,022	911	4,933	-
Net increase (decrease) in cash and cash equivalents	368,343	(50,014)	318,329	-
Cash and cash equivalents, beginning of year	213,732	163,314	377,046	-
Cash and cash equivalents, end of year	\$ 582,075	\$ 113,300	\$ 695,375	\$ -

Non-cash transaction

During the year ended June 30, 2004, the City financed the purchase of a vehicle by obtaining credit in the amount of \$85,698.

Continued...

CITY OF CHEBOYGAN
STATEMENT OF CASH FLOWS
PROPRIETARY FUNDS

FOR THE YEAR ENDED JUNE 30, 2004

	<u>Sewer</u>	<u>Water</u>	<u>Total</u>	<u>Internal Service Fund</u>
Cash flows from operating activities				
Operating income (loss)	\$ 97,850	\$ (44,701)	\$ 53,149	\$ (23,193)
Adjustments to reconcile operating income (loss) to net cash provided by operating activities				
Depreciation	269,993	89,516	359,509	166,620
Changes in operating assets and liabilities which provided (used) cash				
Accounts receivable	(4,627)	(4,751)	(9,378)	-
Prepaid expenses	-	-	-	22,313
Accounts payable	7,078	(30,673)	(23,595)	2,677
Accrued expenses	1,742	1,153	2,895	453
Customer deposits	-	292	292	-
Net cash provided by operating activities	<u>\$ 372,036</u>	<u>\$ 10,836</u>	<u>\$ 382,872</u>	<u>\$ 168,870</u>

Concluded

The accompanying notes are an integral part of these financial statements.

CITY OF CHEBOYGAN
STATEMENT OF FIDUCIARY NET ASSETS
FIDUCIARY FUNDS

JUNE 30, 2004

ASSETS	
Cash and cash equivalents	\$ 4,186
Notes receivable	<u>2,485,000</u>
Total assets	<u>\$ 2,489,186</u>
 LIABILITIES	
Due to other governmental units	\$ 4,186
Deferred revenue	<u>2,485,000</u>
Total liabilities	<u>\$ 2,489,186</u>

The accompanying notes are an integral part of these financial statements.

CITY OF CHEBOYGAN

NOTES TO FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Reporting entity

As required by accounting principles generally accepted in the United States of America, the financial statements of the reporting entity include those of the *City of Cheboygan* (the “City”) and its component unit. The component unit discussed below is included in the City’s reporting entity because of the significance of its operational or financial relationship with the City.

Discretely Presented Component Unit. The Downtown Development Authority (DDA) is reported in a separate column to emphasize that it is legally separate from the City. The members of the governing Board of the Downtown Development Authority are appointed by the City Council. The budgets and expenditures of the Downtown Development Authority must be approved by the City Council. The City also has the ability to significantly influence operations of the Downtown Development Authority. Separate financial statements of the DDA have not been prepared.

B. Government-wide and fund financial statements

The government-wide financial statements (i.e., the statement of net assets and the statement of changes in net assets) report information on all of the nonfiduciary activities of the primary government and its component units. For the most part, the effect of interfund activity has been removed from these statements. *Governmental activities*, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type *activities*, which rely to a significant extent on fees and charges for support. Likewise, the *primary government* is reported separately from certain legally separate *component units* for which the primary government is financially accountable.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment are offset by program revenues. *Direct expenses* are those that are clearly identifiable with a specific function or segment. *Program revenues* include 1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment and 2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. Taxes and other items not properly included among program revenues are reported instead as *general revenues*.

Separate financial statements are provided for governmental funds, proprietary funds, and fiduciary funds, even though the latter are excluded from the government-wide financial statements. Major individual governmental funds and major individual enterprise funds are reported as separate columns in the fund financial statements.

CITY OF CHEBOYGAN

NOTES TO FINANCIAL STATEMENTS

Fund Financial Statements. The fund financial statements provide information about the City's funds, including its fiduciary funds. Separate statements for each fund category – *governmental*, *proprietary* and *fiduciary* – are presented. The emphasis of fund financial statements is on major governmental and enterprise funds, each displayed in a separate column. All remaining governmental funds are aggregated and reported as nonmajor funds.

The City reports the following major governmental funds:

The *General Fund* is the City's primary operating fund. It accounts for all financial resources of the general government, except those required to be accounted for in another fund.

The *Major Street Fund* accounts for the use of motor fuel taxes which are restricted by State statute for major street and highway purposes.

The *2001 Sidwalk Special Assement Bond Fund* accounts for the 2001 special assessment revenues received and the payments on the bonds issued for sidewalk improvements.

The *2000 Special Assessment Streetscape Bond Fund* accounts for the 2000 special assessment revenues received to repay, and the payments on the bonds issued for street improvements.

The *2004 General Obligation Bond Construction Fund* accounts for the bond proceeds received and the construction costs of the City's new public safety building.

The City reports the following major enterprise funds:

The *Sewer Fund* accounts for the activities of the City's sewage disposal and sewer treatment systems.

The *Water Fund* accounts for the activities of the City's water distribution and water treatment system.

Additionally, the City reports the following fund types:

Special Revenue Funds. These funds account for revenue sources that are legally restricted to expenditures for specific purposes not including major capital projects.

Debt Service Funds. These funds account for the resources accumulated and payments made for principal and interest on long-term debt of governmental funds.

CITY OF CHEBOYGAN

NOTES TO FINANCIAL STATEMENTS

Capital Projects Funds. These funds account for the acquisition of capital assets or construction of major capital projects not being financed by proprietary funds.

Internal Service Fund. This fund accounts for operations that provide machinery and equipment to other departments of the City on a cost-reimbursement basis.

Agency Funds. These funds account for assets held for others in an agency capacity.

Measurement focus, basis of accounting, and financial statement presentation

Government-wide, Proprietary and Fiduciary Fund Financial Statements. The government-wide, proprietary and fiduciary fund financial statements are reported using the economic resources measurement focus and the accrual basis of accounting, except for Agency Funds which do not have a measurement focus. Revenues are recorded when earned and expenses are recorded at the time liabilities are incurred, regardless of when the related cash flows take place.

Proprietary fund operating revenues, such as charges for services, result from exchange transactions associated with the principal activity of the fund. Exchange transactions are those in which each party receives and gives up essentially equal values. Nonoperating revenues, such as subsidies and investment earnings, result from nonexchange transactions or ancillary activities.

Nonexchange transactions, in which the City gives (or receives) value without directly receiving (or giving) equal value in exchange, include property taxes, grants and donations. On an accrual basis, revenue from property taxes is recognized in the fiscal year for which the taxes are levied. Revenue from grants and donations is recognized in the fiscal year in which all eligibility requirements have been satisfied.

Governmental Fund Financial Statements. Governmental funds are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Under this method, revenues are recognized when measurable and available. The City considers all revenues reported in the governmental funds to be available if they are collected within 60 days after year-end. Property taxes, state revenue and interest are considered to be susceptible to accrual.

Expenditures are recorded when the related fund liability is incurred, except for principal and interest on long-term debt, compensated absences, and claims and judgments, which are recognized as expenditures to the extent they have matured. Capital asset acquisitions are reported as expenditures in governmental funds. Proceeds of long-term debt and acquisitions under capital leases, if any, are reported as other financing sources.

CITY OF CHEBOYGAN

NOTES TO FINANCIAL STATEMENTS

The government-wide financial statements and proprietary type funds of the City follow private-sector standards of accounting and financial reporting issued prior to December 1, 1989, unless those standards conflict with guidance of the Governmental Accounting Standards Board. Governments also have the option of following subsequent private-sector guidance for their business-type activities and proprietary type funds, subject to this same limitation. The City has elected not to follow subsequent private-sector guidance.

As a general rule the effect of interfund activity has been eliminated from the governmental-wide financial statements. Exceptions to this general rule are payments-in-lieu of taxes and other charges between the government's water and sewer function and various other functions of the government. Elimination of these charges would distort the direct costs and program revenues reported for the various functions concerned.

Amounts reported as *program revenues* include 1) charges to customers or applicants for goods, services, or privileges provided, 2) operating grants and contributions, and 3) capital grants and contributions, including special assessments. Internally dedicated resources are reported as *general revenues* rather than as program revenues. Likewise, general revenues include all taxes.

Proprietary funds distinguish *operating* revenues and expenses from *nonoperating* items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the City's enterprise fund, of the electric enterprise fund, and of the government's internal service funds are charges to customers for sales and services. The City also recognizes as operating revenue the portion of tap fees intended to recover the cost of connecting new customers to the system. Operating expenses for enterprise funds and internal service funds include the cost of sales and services, administrative expenses and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

When both restricted and unrestricted resources are available for use, it is the government's policy to use restricted resources first, then unrestricted resources as they are needed.

D. Assets, liabilities and equity

1. Deposits and investments

The City maintains an investment pool for certain City funds. Each fund's portion of the investment pool is displayed on the statement of net assets/balance sheet as "Cash and cash equivalents". The debt service and trust and agency funds cash resources are invested separately as required by law.

CITY OF CHEBOYGAN

NOTES TO FINANCIAL STATEMENTS

The City's cash and cash equivalents includes cash on hand, demand deposits and short-term investments with original maturities of three months or less from the date of acquisition.

State statutes authorize the City to deposit in the accounts of federally insured banks, credit unions and savings and loan associations and to invest in obligations of the U.S. Treasury, certain commercial paper, repurchase agreements, bankers acceptances, and mutual funds composed of otherwise legal investments.

The City's investments during the year consisted of certificate of deposits.

2. *Receivables and payables*

All receivables are reported at their gross value.

Activity between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as either "due to/from other funds" (i.e., the current portion of interfund loans) or "advances to/from other funds" (i.e., the non-current portion of interfund loans). All other outstanding balances between funds are reported as "due to/from other funds." Any residual balances outstanding between the governmental activities and business-type activities are reported in the government-wide financial statements as "internal balances."

3. *Property taxes*

The City's property taxes are levied each July 1 on the taxable valuation of property located in the City as of the preceding December 31, the lien date. Property taxes are payable without penalty and interest through February 14; as of March 1 of the succeeding year, unpaid real property taxes are sold to and collected by Cheboygan County. Assessed values, as established annually by the City and subject to acceptance by the County, are equalized by the State at an estimated 50% of current market value. The taxable value of real and personal property in the City for the 2003 levy was approximately \$99,500,000. The City's general operating tax rate for fiscal 2003-04 was 14.3543 mills with an additional 3.4 mills for debt.

Property taxes for the DDA are derived by capturing the taxes assessed on the increase in taxable value of the property located within the DDA district.

Property taxes are recognized in the fiscal year in which they are levied.

CITY OF CHEBOYGAN

NOTES TO FINANCIAL STATEMENTS

4. *Capital assets*

Capital assets, which include property, plant, equipment, and infrastructure assets (e.g., roads, sidewalks and similar items), are reported in the applicable governmental or business-type activities columns in the government-wide financial statements. The City defines capital assets as assets with an initial, individual cost of more than \$5,000 and an estimated useful life in excess of two years. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair value at the date of donation.

The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend assets lives are not capitalized.

Major outlays for capital assets and improvements are capitalized as projects are constructed. Interest incurred during the construction phase of capital assets of business-type activities, if any, is included as part of the capitalized value of the assets constructed. No such interest expense was incurred during the current fiscal year.

Capital assets of the primary government are depreciated using the straight-line method over the following estimated useful lives:

	<u>Years</u>
Buildings	15-40
Land improvements	10-40
Sewer and water infrastructure	7-75
Machinery and equipment	3-30
Public domain infrastructure	30

5. *Compensated absences*

It is the City's policy to permit employees to accumulate earned but unused sick and vacation time benefits, subject to certain limitations. All sick and vacation time pay is accrued when incurred in the government-wide statements. A liability for these amounts is reported in governmental funds only if they have matured, for example, as a result of employee resignations or retirements.

CITY OF CHEBOYGAN

NOTES TO FINANCIAL STATEMENTS

6. *Long-term obligations*

In the government-wide financial statements, and proprietary fund types in the fund financial statements, long-term debt and other long-term obligations are reported as liabilities in the applicable governmental activities, business-type activities, or proprietary fund type statement of net assets.

In the fund financial statements, governmental funds report the face amount of debt issued as other financing sources.

7. *Fund balance*

In the fund financial statements, governmental funds report reservations of fund balance for amounts that are not available for appropriation or are legally restricted by outside parties for use for a specific purpose. Designations of fund balance represent tentative management plans that are subject to change.

2. STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

Budgetary information

Annual budgets are adopted on a basis consistent with accounting principles generally accepted in the United States of America for the General and Major Special Revenue Fund. All annual appropriations lapse at fiscal year end.

On or before the second Monday in April of each year, the City Manager must present the proposed budget to the City Council for review. The Council holds public hearings and a final budget is prepared and adopted in June of each year. The City Manager may make transfers of appropriations within a function. Transfers of appropriations between functions require the approval of the City Council. The legal level of budgetary control is the function level.

CITY OF CHEBOYGAN

NOTES TO FINANCIAL STATEMENTS

3. DETAILED NOTES ON ALL FUNDS

A. Deposits and investments

Summary of Deposit and Investment Balances. Following is a reconciliation of deposit and investment balances as of June 30, 2004:

	<u>Primary Government</u>	<u>Component Unit</u>	<u>Total</u>
Statement of Net Assets			
Cash and cash equivalents	\$ 3,394,600	\$ 225,546	\$ 3,620,146
Restricted cash and cash equivalents	41,329	-	41,329
Restricted investments	97,752	-	97,752
Statement of Fiduciary Net Assets			
Cash and cash equivalents	<u>4,186</u>	<u>-</u>	<u>4,186</u>
Total	<u>\$ 3,537,867</u>	<u>\$ 225,546</u>	<u>\$ 3,763,413</u>

At year end, the carrying amount of deposits was \$ 3,763,413. The bank balance was \$3,786,224. Of the bank balance, \$271,178 was covered by Federal Depository Insurance Corporation (FDIC). The remaining balance of \$3,515,046 was uninsured and uncollateralized.

The City believes that due to the dollar amounts of cash deposits and the limits of FDIC insurance, it is impractical to insure all bank deposits. As a result, the City evaluates each financial institution with which it deposits City funds and assesses the level of risk of each institution; only those institutions with an acceptable estimated risk level are used as depositories.

B. Receivables

The composition of receivables is as follows as of June 30, 2004:

	<u>Governmental Activities</u>	<u>Business-type Activities</u>
Accounts receivable	\$ 4,510	\$ 190,825
Special assessment receivable	275,566	-
Due from other governmental units	<u>175,558</u>	<u>-</u>
Total receivables	<u>\$ 455,634</u>	<u>\$ 190,825</u>

CITY OF CHEBOYGAN

NOTES TO FINANCIAL STATEMENTS

Governmental funds report *deferred revenue* in connection with receivables for revenues that are not considered to be available to liquidate liabilities of the current period. At the end of the current fiscal year, *deferred revenue* reported in the governmental funds was \$287,416. Approximately 50% of the total receivables in the governmental activities are not expected to be collected within the next year.

C. Capital assets

Capital assets activity was as follows for the year ended June 30, 2004:

Primary Government

	<u>Beginning Balance</u>	<u>Increases</u>	<u>Ending Balance</u>
Governmental activities			
Capital assets not being depreciated – land	\$ 200,000	\$ -	\$ 200,000
Capital assets being depreciated			
Buildings	4,281,366	26,845	4,308,211
Land improvements	3,170,794	11,051	3,181,845
Equipment	2,827,475	158,973	2,986,448
Infrastructure	<u>2,936,119</u>	<u>-</u>	<u>2,936,119</u>
Total capital assets being depreciated	<u>13,215,754</u>	<u>196,869</u>	<u>13,412,623</u>
Less accumulated depreciation for			
Buildings	(1,023,076)	(105,378)	(1,128,454)
Land improvements	(1,153,588)	(136,209)	(1,289,797)
Equipment	(1,965,010)	(168,061)	(2,133,071)
Infrastructure	<u>(1,164,878)</u>	<u>(97,876)</u>	<u>(1,262,754)</u>
Total accumulated depreciation	<u>(5,306,552)</u>	<u>(507,524)</u>	<u>(5,814,076)</u>
Total capital assets being depreciated, net	<u>7,909,202</u>	<u>(310,655)</u>	<u>7,598,547</u>
Governmental activities capital assets, net	<u>\$ 8,109,202</u>	<u>\$ (310,655)</u>	<u>\$ 7,798,547</u>

CITY OF CHEBOYGAN

NOTES TO FINANCIAL STATEMENTS

	<u>Beginning Balance</u>	<u>Increases</u>	<u>Ending Balance</u>
Business-type activities			
Capital assets not being depreciated – land	\$ 2,251	\$ -	\$ 2,251
Capital assets being depreciated			
Buildings	2,321,996	-	2,321,996
Sewer system	7,210,021	12,179	7,222,200
Water system	4,946,752	65,619	5,012,371
Machinery and equipment	<u>2,729,755</u>	<u>-</u>	<u>2,729,755</u>
Total capital assets being depreciated	<u>17,208,524</u>	<u>77,798</u>	<u>17,286,322</u>
Less accumulated depreciation for			
Buildings	(1,449,692)	(58,048)	(1,507,740)
Sewer system	(1,796,216)	(111,896)	(1,908,112)
Water system	(1,349,974)	(89,516)	(1,439,490)
Machinery and equipment	<u>(2,201,194)</u>	<u>(100,049)</u>	<u>(2,301,243)</u>
Total accumulated depreciation	<u>(6,797,076)</u>	<u>(359,509)</u>	<u>(7,156,585)</u>
Total capital assets being depreciated, net	<u>10,411,448</u>	<u>(281,711)</u>	<u>10,129,737</u>
Business-type activities capital assets, net	<u>\$10,413,699</u>	<u>\$ (281,711)</u>	<u>\$10,131,988</u>
<u>Component unit</u>			
Capital assets not being depreciated – land	<u>\$ 150,000</u>	<u>\$ -</u>	<u>\$ 150,000</u>

CITY OF CHEBOYGAN

NOTES TO FINANCIAL STATEMENTS

Depreciation expense was charged to functions/programs of the primary government as follows:

Governmental activities

Public works	\$ 201,932
Recreation and culture	68,297
General government	68,421
Public safety	2,254
Capital assets held by the government's internal service funds are charged to the various functions based on their usage of the assets	<u>166,620</u>

Total depreciation expense – governmental activities **\$ 507,524**

Business-type activities

Sewer	\$ 269,993
Water	<u>89,516</u>

Total depreciation expense – business-type activities **\$ 359,509**

D. Accounts payable and accrued expenses

The composition of accounts payable and accrued expenses is as follows as of June 30, 2004:

	<u>Governmental Activities</u>	<u>Business-type Activities</u>	<u>Component Unit</u>
Accounts payable	\$ 45,127	\$ 24,021	\$ 837
Accrued expenses	118,352	2,895	240
Due to other governmental units	<u>11,624</u>	<u>-</u>	<u>-</u>
Total payables and accrued expenses	<u>\$ 175,103</u>	<u>\$ 29,916</u>	<u>\$ 1,077</u>

CITY OF CHEBOYGAN

NOTES TO FINANCIAL STATEMENTS

E. Interfund receivables, payables and transfers

Interfund transfers consisted of transfers out of the following funds and into nonmajor governmental funds for the year ended June 30, 2004:

General Fund	\$ 262,306
Major Street Fund	111,984
Sewer Fund	16,625
Water Fund	11,000
Internal Services Fund	3,800
Nonmajor governmental funds	<u>71,274</u>

Total transfers **\$ 476,989**

Transfers are used to (1) move revenues from the fund that is required to collect them to the fund that is required or allowed to expend them, (2) move receipts restricted to or allowed for debt service from the funds collecting the receipts to the debt service fund as debt service payments become due, and (3) use unrestricted revenues collected in the General Fund to finance various programs accounted for in other funds in accordance with budgetary authorizations.

F. Long-term debt

A summary of long-term debt and transactions related thereto is as follows for the year ended June 30, 2004:

	<u>Balance</u> <u>July 1,</u> <u>2003</u>	<u>Additions</u>	<u>(Reductions)</u>	<u>Balance</u> <u>June 30,</u> <u>2004</u>	<u>Due</u> <u>Within</u> <u>1 Year</u>
Governmental activities					
Bonds payable					
1997 Water and Sanitary Sewer System Improvement General Obligation Bonds maturing serially to 2022 in annual amounts ranging from \$35,000 to \$285,000 and bearing interest ranging from 5.0% to 7.5%.	\$ 2,845,000	\$ -	\$ (50,000)	\$ 2,795,000	\$ 55,000

CITY OF CHEBOYGAN

NOTES TO FINANCIAL STATEMENTS

	<u>Balance July 1, 2003</u>	<u>Additions</u>	<u>(Reductions)</u>	<u>Balance June 30, 2004</u>	<u>Due Within 1 Year</u>
1997 Rural Economic Development Bonds maturing serially to 2037 in annual amounts ranging from \$23,000 to \$108,000 and bearing interest at 4.5%.	\$ 1,875,000	\$ -	\$ (24,000)	\$ 1,851,000	\$ 26,000
2004 General Obligation Bonds. Bonds maturing serially to 2023 in annual payments ranging from \$25,000 to \$ 105,000 and bearing interest of 3.25% to 5.15%.		- 1,350,000	-	1,350,000	25,000
2002 Major and Local Street General Obligation Bonds maturing serially to 2012 in annual amounts ranging from \$25,000 to \$45,000 and bearing interest at 3.95%	325,000	-	(30,000)	295,000	30,000
2000 Streetscape Improvement Tax Increment Financing Bonds maturing serially to 2005 in annual amounts ranging from \$100,000 to \$120,000 and bearing interest ranging from 4.6% to 7.0%.	240,000	-	(120,000)	120,000	120,000
1997 Michigan Transportation Fund Bonds maturing serially to 2012 in annual amounts ranging from \$20,000 to \$30,000 and bearing interest ranging from 4.8% to 5.8%.	220,000	-	(20,000)	200,000	20,000

CITY OF CHEBOYGAN

NOTES TO FINANCIAL STATEMENTS

	<u>Balance July 1, 2003</u>	<u>Additions</u>	<u>(Reductions)</u>	<u>Balance June 30, 2004</u>	<u>Due Within 1 Year</u>
2000 Special Assessment Streetscape Bonds maturing serially to 2010 in annual amounts ranging from \$20,000 to \$30,000 and bearing interest ranging from 5.0% to 7.0%.	\$ 180,000	\$ -	\$ (25,000)	\$ 155,000	\$ 25,000
1998 Local Street Paving Bonds maturing serially to 2009 in annual amounts ranging from \$20,000 to \$30,000 and bearing interest ranging from 4.1% to 4.7%.	160,000	-	(25,000)	135,000	25,000
2001 Sidewalk Improvement General Obligation Bonds maturing serially to 2011 in annual amounts ranging from \$4,000 to \$10,000 and bearing interest at 4.15%.	83,000	-	(5,000)	78,000	8,000
2001 Sidewalk Improvement Special Assessment Limited Tax General Obligation Bonds maturing serially to 2011 in annual amounts ranging from \$3,000 to \$10,000 and bearing interest at 4.15%.	58,000	-	(3,000)	55,000	5,000
1992 Building Authority Bonds (Pavilion) repaid during 2004.	<u>40,000</u>	<u>-</u>	<u>(40,000)</u>	<u>-</u>	<u>-</u>
Total bonds payable	<u>6,026,000</u>	<u>1,350,000</u>	<u>(342,000)</u>	<u>7,034,000</u>	<u>339,000</u>

CITY OF CHEBOYGAN

NOTES TO FINANCIAL STATEMENTS

	<u>Balance July 1, 2003</u>	<u>Additions</u>	<u>(Reductions)</u>	<u>Balance June 30, 2004</u>	<u>Due Within 1 Year</u>
Notes payable and other					
2000 Equipment note payable with annual payments of \$25,628 including interest at 5.48%.	\$ 127,560	\$ -	\$ (18,465)	\$ 109,095	\$ 19,503
2003 Equipment note payable with annual payments of \$22,260 including interest at 2.691%.	84,606	-	(20,035)	64,571	20,860
2003 Equipment note payable with annual payments of \$22,313 including interest at 6.75%.	58,824	-	(18,342)	40,482	19,580
2003 Equipment note payable with annual payments of \$16,897 including interest at 5.95%.	45,208	-	(14,207)	31,001	15,053
2001 Equipment note payable with annual payments of \$19,075 including interest at 6.40%.	34,777	-	(16,849)	17,928	17,928
2001 Equipment note payable with monthly payments of \$274 including interest at 9.98%.	6,144	-	(2,542)	3,602	3,061

CITY OF CHEBOYGAN

NOTES TO FINANCIAL STATEMENTS

	<u>Balance July 1, 2003</u>	<u>Additions</u>	<u>(Reductions)</u>	<u>Balance June 30, 2004</u>	<u>Due Within 1 Year</u>
2004 GMC Top Kick note payable with monthly payments ranging from \$18,751 to \$18,724, including interest of 3.042%.	\$ -	\$ 85,698	\$ -	\$ 85,698	\$ 16,108
Accumulated sick and vacation pay	<u>225,444</u>	<u>9,649</u>	<u>-</u>	<u>235,093</u>	<u>22,494</u>
Total notes payable and other	<u>357,119</u>	<u>85,698</u>	<u>(90,440)</u>	<u>587,470</u>	<u>134,587</u>
Total long-term debt	<u>\$6,383,119</u>	<u>\$1,435,698</u>	<u>\$(432,440)</u>	<u>\$7,621,470</u>	<u>\$473,587</u>

For the governmental activities, compensated absences are generally liquidated by the General Fund.

Annual debt service requirements to maturity for the above obligations except for the liability for accrued compensated absences is as follows:

	<u>Governmental activities</u>	
	<u>Principal</u>	<u>Interest</u>
2005	\$ 451,093	\$ 348,124
2006	337,014	330,698
2007	319,140	314,993
2008	319,598	300,917
2009	347,533	286,040
2010-2014	1,394,000	1,214,693
2015-2019	1,595,000	864,550
2020-2024	1,569,000	393,108
2025-2029	335,000	208,350
2030-2034	417,000	125,910
2035-2037	<u>301,999</u>	<u>27,765</u>
	<u>\$7,386,377</u>	<u>\$4,415,148</u>

Total interest expense for the City for the year was \$313,877.

CITY OF CHEBOYGAN

NOTES TO FINANCIAL STATEMENTS

	<u>Balance</u> <u>July 1,</u> <u>2003</u>	<u>Additions</u>	<u>(Reductions)</u>	<u>Balance</u> <u>June 30,</u> <u>2004</u>	<u>Due</u> <u>Within</u> <u>1 Year</u>
Component unit					
1994 Urban Land loan payable with annual payments of \$13,300 through 2005, 0% interest.	\$ 26,600	\$ -	\$ (13,300)	\$ 13,300	\$ 13,300

G. Restatements

As of and for the year ended June 30, 2004, the City implemented the following Governmental Accounting Standards Board pronouncements:

Statements

- No. 34 – *Basic Financial Statements – and Management’s Discussion and Analysis – for State and Local Governments*
- No. 37 – *Basic Financial Statements – and Management’s Discussion and Analysis – for State and Local Governments: Omnibus*
- No. 38 – *Certain Financial Statement Note Disclosures*

Interpretation

- No. 6 – *Recognition and Measurement of Certain Liabilities and Expenditures in Governmental Fund Financial Statements*

The above pronouncements are all related to the new financial reporting requirements for all state and local governments. These pronouncements are scheduled for a phased implementation (based on the size of the government) through fiscal years ending in 2005. The City was required to implement the new requirements as of and for the year ended June 30, 2004.

The more significant of the changes required by the new standards include:

- Management’s discussion and analysis
- Basic financial statements that include:
 - Government-wide financial statements, prepared using the economic resources measurement focus and the accrual basis of accounting;

CITY OF CHEBOYGAN

NOTES TO FINANCIAL STATEMENTS

- Fund financial statements, consisting of a series of statements that focus on a government's major governmental funds and enterprise funds;
- Schedules to reconcile the fund financial statements to the government-wide financial statements;
- Notes to the basic financial statement

As a result of implementing these pronouncements for the fiscal year ended June 30, 2004, the following restatements were made to beginning net asset accounts in the government-wide financial statements.

Beginning net assets for governmental activities was determined as follows:

Fund balances of general, special revenue, debt service, and capital project funds as of June 30, 2003	\$ 1,524,683
Add: governmental capital assets, including general fixed assets and infrastructure as of June 30, 2003	10,476,639
Deduct: accumulated depreciation as of June 30, 2003 on above governmental capital assets	(3,258,614)
Add: governmental internal service funds net assets as of June 30, 2003	553,090
Add: deferred revenue on special assessments as of June 30, 2003	313,541
Deduct: general obligation bonds payable as of June 30, 2003	(6,026,000)
Deduct: accrued interest payable on debt as of June 30, 2003	(73,745)
Deduct: governmental compensated absences payable as of June 30, 2003	<u>(225,444)</u>
Governmental activities net assets, restated, as of June 30, 2003	<u>\$ 3,284,150</u>

CITY OF CHEBOYGAN

NOTES TO FINANCIAL STATEMENTS

Beginning net assets for the component unit was determined as follows:

Fund balance of the component unit as of June 30, 2003	\$ 217,267
Add: governmental capital assets, including general fixed assets and infrastructure as of June 30, 2003	150,000
Deduct: general obligation bonds, installment contracts and loans payable as of June 30, 2003	<u>(26,600)</u>
Component unit net assets, restated, as of June 30, 2003	<u>\$ 340,667</u>

Beginning net assets of the enterprise funds were derived by aggregating the previously reported retained earnings and contributed capital of those funds.

4. OTHER INFORMATION

A. Defined Benefit Pension Plan

Plan Description

The City's defined benefit pension plan provides retirement, death and disability benefits to plan members and beneficiaries. The City participates in the Municipal Employees Retirement System of Michigan (MERS), an agent multiple-employer plan administered by the MERS Retirement Board. Act No. 427 of the Public Acts of 1984, as amended, establishes and amends the benefit provisions of the participants in MERS. The Municipal Employees Retirement System of Michigan issues a publicly available financial report that includes financial statements and required supplementary information for MERS. That report may be obtained by writing to the Municipal Employees Retirement System of Michigan, 447 N. Canal Road, Lansing, Michigan 48917 or by calling (800) 767-6377.

Funding Policy

The City is required to contribute at an actuarially determined rate; the current rate ranges from 7.33% to 13.07% of annual covered payroll. City employees are required to contribute 3% of the first \$4,200 of annual compensation and 5% of portions over \$4,200. The contribution requirements of the City are established and may be amended by the Retirement Board of MERS. The contribution requirements of plan members are established and may be amended by the City, depending on the MERS contribution program adopted by the City.

CITY OF CHEBOYGAN

NOTES TO FINANCIAL STATEMENTS

Annual Pension Cost

For the year ended June 30, 2004, the City's annual pension cost of \$119,970 for MERS was equal to the City's required and actual contributions. The required contribution was determined using the entry age actuarial cost method. The actuarial assumptions included (a) a rate of return on the investment of present and future assets of 8%, (b) additional projected salary increases up to 4.2% per year, depending on age, attributable to seniority/merit, and (c) an inflationary rate of 4.5%. The actuarial value of MERS assets was determined on the basis of a valuation method that assumes the fund earns the expected rate of return, and includes an adjustment to reflect fair value. The City's unfunded actuarial accrued liability is being amortized as a level percentage of projected payroll on an open basis. The remaining amortization period at December 31, 2003, the date of the last actuarial valuation, was 30 years.

Three-year Trend Information

<u>Fiscal Year Ending</u>	<u>Annual Pension Cost (APC)</u>	<u>Percentage of APC Contributed</u>	<u>Net Pension Obligation</u>
6/30/02	\$ 109,131	100%	-
6/30/03	88,119	100	-
6/30/04	119,970	100	-

Schedule of Funding Progress

<u>Actuarial Valuation Date</u>	<u>Actuarial Value of Assets (a)</u>	<u>Actuarial Accrued Liability (AAL) -Entry Age (b)</u>	<u>Unfunded AAL (UAAL) (b-a)</u>	<u>Funded Ratio (a/b)</u>	<u>Covered Payroll (c)</u>	<u>UAAL as a Percentage of Covered Payroll ((b-a)/c)</u>
12/31/98	\$4,161,553	\$ 4,702,041	\$ 540,488	89%	\$1,020,672	53%
12/31/99	4,718,894	5,131,625	412,731	92	1,171,684	35
12/31/00	5,070,923	5,587,263	516,340	91	1,104,909	47
12/31/01	5,328,539	6,125,340	796,801	87	1,230,873	65
12/31/02	5,346,218	6,463,306	1,117,088	83	1,341,615	83
12/31/03	5,608,877	6,665,885	1,057,008	84	1,291,949	82

CITY OF CHEBOYGAN

NOTES TO FINANCIAL STATEMENTS

B. Other Post Retirement Benefits

In addition to the pension benefits described in Note 4A, the City provides post retirement health care benefits, in accordance with City policy, to all employees as of June 30, 1999 who retire from the City on or after attaining age 55 with 25 years of service or retirement at age 62. Currently six employees meet those eligibility requirements. The City will pay up to 100% of the employees health insurance cost including spousal coverage. Expenditures for post retirement healthcare benefits are recognized as incurred. During the fiscal year ended June 30, 2004, expenditures of \$52,000 were recognized for post retirement healthcare.

C. Accumulated Sick and Vacation Pay

Employees of the City earn sick and vacation time at varying rates based on the following:

Under the terms of the Police and AFCSME union contract (DPW, Sewer and clerical employees), sick leave is accumulated at the rate of one day for each month of service, with a maximum accumulation of sixty days. Employees who have accumulated more than 60 days will not be allowed additional accumulation. Upon retirement or death, employees will be paid three full days' pay times the number of years of continuous service with a maximum of 100 days.

As a result of separation for any other reason, the employee will lose all accumulated sick leave.

City management personnel earn sick leave at a rate of 8 hours per month of service. All unused sick time is paid out, generally, in November of each year at 50% of the employees current rate of pay.

Vacation leave is earned based on the following schedule for all employees:

<u>Years of Service</u>	<u>Vacation Days</u>
1	2 weeks
5	3 weeks
10	4 weeks
20	4 weeks plus 1/2 day for each year beyond 20 years

No more than 50% of an employee's annual vacation leave may be carried over to the next employment year and no accumulation is allowed beyond six weeks of annual leave.

CITY OF CHEBOYGAN

NOTES TO FINANCIAL STATEMENTS

The accumulated sick and vacation pay liability is \$235,093 at June 30, 2004. The City has established a Termination Liability Special Revenue Fund to accumulate amounts necessary to cover this liability as it becomes due. The balance in the Termination Liability Fund at June 30, 2004 is \$119,378.

D. Risk Management and Litigation

The City is exposed to various risks of losses related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters for which it obtains coverage from commercial insurance companies. The City has had no settled claims resulting from these risks that exceeded their commercial coverage in any of the past three fiscal years.

E. Economic Development Project

On August 6, 1994, the City borrowed \$3,000,000 from the United States Department of Housing and Urban Development (HUD) under the provisions of Section 108 of the Housing and Community Development Act of 1974, as amended, for the Great Lakes Tissue Company Project. This loan was used to assist the Great Lakes Tissue Company in connection with the purchase of the former Proctor & Gamble Company facility.

On September 17, 1994 Great Lakes Tissue Company signed a note receivable with the City of Cheboygan for \$3,000,000 representing amounts owed to the City from Great Lakes Tissue Company for the economic development project designed to establish additional employment in the City of Cheboygan. The outstanding note receivable balance as of June 30, 2004 is \$2,485,000. Because this receivable is not available for use by the City, deferred revenue has been recorded, in the amount of \$2,485,000, to offset the receivable balance.

The loan consists of a series of notes ranging in amounts from \$100,000 to \$305,000, with maturity dates from August 1, 1995 to August 1, 2008, due with interest ranging from 3.82% to 6.93%. The outstanding loan balance, payable to HUD at June 30, 2004 is \$2,485,000. No payments were made during fiscal year end June 30, 2004. The loan is secured by a second priority security interest covering all machinery and equipment and second priority mortgage covering all real property. The loan is to be repaid with principal and interest payments received from Great Lakes Tissue Company and is guaranteed by the City's future Community Development Block Grant entitlement. Neither the full faith and credit nor the taxing power of the City is pledged for the payment of the notes. Since the debt payments are being made by Great Lakes Tissue Company, the debt has not been recorded by the City. Future principal maturities are scheduled as follows: \$305,000 in 2005 through 2008 and the balance of \$1,265,000 is due during fiscal 2009.

SUPPLEMENTARY INFORMATION

CITY OF CHEBOYGAN

SCHEDULE OF REVENUES

BUDGET AND ACTUAL - GENERAL FUND

FOR THE YEAR ENDED JUNE 30, 2004

	Budget			Variance with Amended Budget Positive (Negative)
	Original	Amended	Actual	
Taxes				
Current property taxes	\$ 1,266,700	\$ 1,314,400	\$ 1,315,776	\$ 1,376
Payments in lieu of taxes	7,600	7,600	5,968	(1,632)
Special assessments	16,000	15,000	10,660	(4,340)
Interest and penalties on delinquent taxes	9,200	16,600	26,387	9,787
Total taxes	1,299,500	1,353,600	1,358,791	5,191
Licenses and permits	8,000	9,000	10,759	1,759
Federal revenues				
DEQ grant	105,000	-	-	-
COPS FAST grant	-	-	968	968
Total federal revenues	105,000	-	968	968
State revenues				
Sales tax	634,800	667,300	668,575	1,275
Police training	2,000	2,000	2,103	103
Liquor licenses	7,650	6,900	6,631	(269)
Total state revenues	644,450	676,200	677,309	1,109
Charges for services				
Property tax administration fees	43,000	22,000	22,665	665
Parking and dock fees	9,000	5,400	4,809	(591)
Total charges for services	52,000	27,400	27,474	74
Interest	13,000	11,000	15,217	4,217
Miscellaneous revenue	50,000	69,600	60,672	(8,928)
Total revenues	\$ 2,171,950	\$ 2,146,800	\$ 2,151,190	\$ 4,390

CITY OF CHEBOYGAN

SCHEDULE OF EXPENDITURES AND OTHER FINANCING USES - BUDGET AND ACTUAL GENERAL FUND

FOR THE YEAR ENDED JUNE 30, 2004

	Budget		Actual	Variance With Amended Budget Positive (Negative)
	Original	Amended		
Legislative				
City council	\$ 42,000	\$ 46,575	\$ 46,575	\$ -
General government				
City manager	124,430	138,600	137,338	1,262
Clerk - treasurer	179,150	165,400	160,616	4,784
Clerk - elections	14,250	18,200	5,923	12,277
Assessor	83,820	77,200	71,083	6,117
Board of review	4,000	4,300	4,379	(79)
City hall and grounds	109,550	116,200	131,882	(15,682)
Total general government	515,200	519,900	511,221	8,679
Public safety				
Police department	764,650	759,440	756,477	2,963
Fire department	72,310	98,910	92,000	6,910
Parking	15,550	15,150	15,270	(120)
Total public safety	852,510	873,500	863,747	9,753
Public works				
Public works	128,140	184,182	184,156	26
Street lighting	58,000	58,000	58,026	(26)
Total public works	186,140	242,182	242,182	-
Culture and recreation				
Recreation department	382,475	219,525	220,549	(1,024)
Opera house	20,000	20,000	5,600	14,400
Soccer field	-	-	256	(256)
Christmas decorations	500	-	-	-
Humane society	6,000	6,000	6,000	-
Promotion	7,000	7,000	7,000	-
Beautification	2,000	500	180	320
Total culture and recreation	417,975	253,025	239,585	13,440
Total expenditures	2,013,825	1,935,182	1,903,310	31,872
Other financing uses				
Transfers out	349,645	265,322	262,306	3,016
Total expenditures and other uses	\$ 2,363,470	\$ 2,200,504	\$ 2,165,616	\$ 34,888

CITY OF CHEBOYGAN
COMBINING BALANCE SHEET
NONMAJOR GOVERNMENTAL FUNDS

JUNE 30, 2004

	Special Revenue Funds	Debt Service Funds	Capital Project Funds
ASSETS			
Cash and cash equivalents	\$ 372,247	\$ 98,309	\$ 11,416
Accounts receivable	324	-	-
Due from other governmental units	23,236	-	-
Restricted cash	-	-	-
Restricted investments	-	-	-
Total assets	<u>\$ 395,807</u>	<u>\$ 98,309</u>	<u>\$ 11,416</u>
LIABILITIES AND FUND BALANCES			
Liabilities			
Accounts payable	\$ 4,428	\$ -	\$ -
Accrued expenses	531	-	-
Total liabilities	<u>4,959</u>	<u>-</u>	<u>-</u>
Fund balances			
Reserved for			
Termination liability	119,378	-	-
Retiree BC/BS	212,455	-	-
Perpetual care	-	-	-
Debt service	-	98,309	-
Capital projects	-	-	11,416
Unreserved, undesignated	59,015	-	-
Total fund balances	<u>390,848</u>	<u>98,309</u>	<u>11,416</u>
Total liabilities and fund balances	<u>\$ 395,807</u>	<u>\$ 98,309</u>	<u>\$ 11,416</u>

Permanent Trust Fund	Total
\$ -	\$ 481,972
-	324
-	23,236
41,329	41,329
97,752	97,752
\$ 139,081	\$ 644,613

\$ -	\$ 4,428
-	531
-	4,959

-	119,378
-	212,455
139,081	139,081
-	98,309
-	11,416
-	59,015
139,081	639,654
\$ 139,081	\$ 644,613

CITY OF CHEBOYGAN

COMBINING STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES NONMAJOR GOVERNMENTAL FUNDS

FOR THE YEAR ENDED JUNE 30, 2004

	Special Revenue Funds	Debt Service Funds	Capital Project Funds
Revenues			
Taxes	\$ -	\$ 314,275	\$ -
State revenues	156,223	-	-
Charges for services	14,600	-	-
Interest	6,102	5,406	130
Miscellaneous	15,810	-	-
Total revenues	192,735	319,681	130
Expenditures			
Current			
General government	157,817	-	-
Public works	237,379	-	-
Capital projects	-	-	11,051
Debt service			
Principal retirement	-	314,000	-
Interest and fiscal charges	-	283,792	-
Total expenditures	395,196	597,792	11,051
Revenues over (under) expenditures	(202,461)	(278,111)	(10,921)
Other financing sources (uses)			
Transfers in	321,500	155,489	-
Transfers out	(71,274)	-	-
Transfer in from component unit	-	131,400	-
Total other financing sources (uses)	250,226	286,889	-
Net change in fund balances	47,765	8,778	(10,921)
Fund balances, beginning of year	343,083	89,531	22,337
Fund balances, end of year	\$ 390,848	\$ 98,309	\$ 11,416

Permanent Trust Fund	Total
\$ -	\$ 314,275
-	156,223
-	14,600
1,848	13,486
1,800	17,610
3,648	516,194
-	157,817
-	237,379
-	11,051
-	314,000
-	283,792
-	1,004,039
3,648	(487,845)
-	476,989
-	(71,274)
-	131,400
-	537,115
3,648	49,270
135,433	590,384
\$ 139,081	\$ 639,654

CITY OF CHEBOYGAN
COMBINING BALANCE SHEET
NONMAJOR SPECIAL REVENUE FUNDS

JUNE 30, 2004

ASSETS	Local Street	Cemetery	Retiree BC/BS Investment Fund	PA 222 Liability
Cash and cash equivalents	\$ (10,719)	\$ 102	\$ 212,455	\$ 51,031
Accounts receivable	-	324	-	-
Due from other governmental units	23,236	-	-	-
Total assets	\$ 12,517	\$ 426	\$ 212,455	\$ 51,031
LIABILITIES AND FUND BALANCES				
Liabilities				
Accounts payable	\$ 4,428	\$ -	\$ -	\$ -
Accrued expenses	531	-	-	-
Total liabilities	4,959	-	-	-
Fund balances				
Fund balances				
Reserved				
Retiree BC/BS	-	-	212,455	-
Termination liability	-	-	-	-
Unreserved				
Undesignated	7,558	426	-	51,031
Total fund balances	7,558	426	212,455	51,031
Total liabilities and fund balances	\$ 12,517	\$ 426	\$ 212,455	\$ 51,031

Termination Liability	Total
\$ 119,378	\$ 372,247
-	324
-	23,236
\$ 119,378	\$ 395,807

\$ -	\$ 4,428
-	531
-	4,959

-	212,455
119,378	119,378
-	59,015
119,378	390,848
\$ 119,378	\$ 395,807

CITY OF CHEBOYGAN

COMBINING STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES NONMAJOR SPECIAL REVENUE FUNDS

FOR THE YEAR ENDED JUNE 30, 2004

	Local Street	Cemetery	Retiree BC/BS Investment Fund	PA 222 Liability
Revenues				
State revenues	\$ 156,223	\$ -	\$ -	\$ -
Charges for services	3,500	11,100	-	-
Interest	-	992	3,006	461
Miscellaneous	-	250	-	-
Total revenues	159,723	12,342	3,006	461
Expenditures				
Current				
General government	-	67,316	52,000	2,282
Public works	237,379	-	-	-
Total expenditures	237,379	67,316	52,000	2,282
Revenues over (under) expenditures	(77,656)	(54,974)	(48,994)	(1,821)
Other financing sources (uses)				
Transfers in	154,000	55,000	105,000	7,500
Transfers out	(71,274)	-	-	-
Total other financing sources (uses)	82,726	55,000	105,000	7,500
Net change in fund balances	5,070	26	56,006	5,679
Fund balances, beginning of year	2,488	400	156,449	45,352
Fund balances, end of year	\$ 7,558	\$ 426	\$ 212,455	\$ 51,031

Termination Liability	Total
\$ -	\$ 156,223
-	14,600
1,643	6,102
15,560	15,810
17,203	192,735
36,219	157,817
-	237,379
36,219	395,196
(19,016)	(202,461)
-	321,500
-	(71,274)
-	250,226
(19,016)	47,765
138,394	343,083
\$ 119,378	\$ 390,848

CITY OF CHEBOYGAN
COMBINING BALANCE SHEET
NONMAJOR DEBT SERVICE FUNDS

JUNE 30, 2004

ASSETS	1992 Pavilion Bonds I	1992 Pavilion Bonds II	1996 Street Paving Bonds	1997 Water/Sewer Improvement Bonds	1997 Rural Economic Development Loan
Cash and cash equivalents (equal to fund balances)	\$ -	\$ 5,466	\$ -	\$ 50,223	\$ 38,990

1998 Local Street Paving Bond	1996 Street Paving Bonds	2001 Sidewalk General Obligation Bond	2000 DDA TIF Bond	2002 Transportation Bond	2004 General Obligation Bond	Total
<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 3,630</u>	<u>\$ 98,309</u>

CITY OF CHEBOYGAN

COMBINING STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES NONMAJOR DEBT SERVICE FUNDS

FOR THE YEAR ENDED JUNE 30, 2004

	1992 Pavilion Bonds I	1992 Pavilion Bonds II	1996 Street Paving Bonds	1997 Water/Sewer Improvement Bonds	1997 Rural Economic Development Loan
Revenues					
Taxes	\$ -	\$ 133	\$ -	\$ 203,707	\$ 110,435
Interest	-	48	-	1,137	591
Total revenues	-	181	-	204,844	111,026
Expenditures					
Debt service					
Principal retirement	40,000	-	-	50,000	24,000
Interest and fiscal charges	1,170	-	-	152,663	84,240
Total expenditures	41,170	-	-	202,663	108,240
Revenues over (under) expenditures	(41,170)	181	-	2,181	2,786
Other financing sources (uses)					
Transfers in	41,170	-	-	-	-
Transfers in from component unit	-	-	-	-	-
Total other financing sources (uses)	41,170	-	-	-	-
Net change in fund balances	-	181	-	2,181	2,786
Fund balances, beginning of year	-	5,285	-	48,042	36,204
Fund balances, end of year	\$ -	\$ 5,466	\$ -	\$ 50,223	\$ 38,990

1998 Local Street Paving Bond	1996 Street Paving Bonds	2001 Sidewalk General Obligation Bond	2000 DDA TIF Bond	2002 Transportation Bond	2004 General Obligation Bond	Total
\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 314,275
-	-	-	-	-	3,630	5,406
-	-	-	-	-	3,630	319,681
25,000	20,000	5,000	120,000	30,000	-	314,000
6,680	11,460	3,341	11,400	12,838	-	283,792
31,680	31,460	8,341	131,400	42,838	-	597,792
(31,680)	(31,460)	(8,341)	(131,400)	(42,838)	3,630	(278,111)
31,680	31,460	8,341	-	42,838	-	155,489
-	-	-	131,400	-	-	131,400
31,680	31,460	8,341	131,400	42,838	-	286,889
-	-	-	-	-	3,630	8,778
-	-	-	-	-	-	89,531
\$ -	\$ -	\$ -	\$ -	\$ -	\$ 3,630	\$ 98,309

CITY OF CHEBOYGAN
COMBINING BALANCE SHEET
NONMAJOR CAPITAL PROJECT FUNDS

JUNE 30, 2004

ASSETS	2001 Sidewalk Improvement Fund	2002 Street Construction Fund	Total
	<u> </u>	<u> </u>	<u> </u>
Cash and cash equivalents (equal to fund balances)	\$ 7,123	\$ 4,293	\$ 11,416
	<u> </u>	<u> </u>	<u> </u>

CITY OF CHEBOYGAN

**COMBINING STATEMENT OF REVENUES, EXPENDITURES
AND CHANGES IN FUND BALANCES
NONMAJOR CAPITAL PROJECT FUNDS**

FOR THE YEAR ENDED JUNE 30, 2004

	2001 Sidewalk Improvement Fund	2002 Street Construction Fund	Total
Revenues			
Interest	\$ 91	\$ 39	\$ 130
Expenditures			
Capital outlay	11,051	-	11,051
Net change in fund balances	(10,960)	39	(10,921)
Fund balances, beginning of year	18,083	4,254	22,337
Fund balances, end of year	\$ 7,123	\$ 4,293	\$ 11,416

CITY OF CHEBOYGAN

COMBINING STATEMENT OF CHANGES IN ASSETS AND LIABILITIES ALL AGENCY FUNDS

FOR THE YEAR ENDED JUNE 30, 2004

	Balance July 1, 2003	Additions	Deductions	Balance June 30, 2004
CURRENT TAX COLLECTION FUND				
ASSETS				
Cash and cash equivalents	\$ 2,875	\$ 4,171,125	\$ (4,169,814)	\$ 4,186
LIABILITIES				
Due to other funds	\$ 2,875	\$ 1,736,690	\$ (1,739,565)	\$ -
Due to other governmental units	-	2,434,435	(2,430,249)	4,186
Total liabilities	\$ 2,875	\$ 4,171,125	\$ (4,169,814)	\$ 4,186
HUD LOAN				
ASSETS				
Notes receivable	\$ 2,485,000	\$ -	\$ -	\$ 2,485,000
LIABILITIES				
Deferred revenue	\$ 2,485,000	\$ -	\$ -	\$ 2,485,000
TOTAL AGENCY FUNDS				
ASSETS				
Cash and cash equivalents	\$ 2,875	\$ 4,171,125	\$ (4,169,814)	\$ 4,186
Notes receivable	2,485,000	-	-	2,485,000
Total assets	\$ 2,487,875	\$ 4,171,125	\$ (4,169,814)	\$ 2,489,186
LIABILITIES				
Due to other funds	\$ 2,875	\$ 1,736,690	\$ (1,739,565)	\$ -
Due to other governmental units	-	2,434,435	(2,430,249)	4,186
Deferred revenue	2,485,000	-	-	2,485,000
Total liabilities	\$ 2,487,875	\$ 4,171,125	\$ (4,169,814)	\$ 2,489,186

CITY OF CHEBOYGAN
BALANCE SHEET AND STATEMENT OF NET ASSETS
COMPONENT UNIT

JUNE 30, 2004

	Downtown Development Authority	Adjustments	Statement of Net Assets
Assets			
Cash and cash equivalents	\$ 225,546	\$ -	\$ 225,546
Capital assets, net of depreciaton	-	150,000	150,000
Total assets	<u>\$ 225,546</u>	<u>150,000</u>	<u>375,546</u>
Liabilities			
Accounts payable	\$ 837	-	837
Accrued expenses	240	-	240
Long term debt due within one year	-	13,300	13,300
Total liabilities	<u>1,077</u>	<u>13,300</u>	<u>14,377</u>
Fund balance			
Unreserved	224,469	(224,469)	-
Total liabilities and fund balance	<u>\$ 225,546</u>		
Net assets			
Invested in capital assets, net of related debt		136,700	136,700
Unrestricted		224,469	224,469
Total net assets		<u>\$ 361,169</u>	<u>\$ 361,169</u>

CITY OF CHEBOYGAN

STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE AND STATEMENT OF ACTIVITIES COMPONENT UNIT

FOR THE YEAR ENDED JUNE 30, 2004

	Downtown Development Authority	Adjustments	Statement of Activities
Revenues			
Property taxes	\$ 155,342	\$ -	\$ 155,342
Interest	1,869	-	1,869
Total revenues	157,211	-	157,211
Expenditures / expenses			
Current			
Public works	5,309	-	5,309
Debt service			
Principal	13,300	(13,300)	-
Total expenditures / expenses	18,609	(13,300)	5,309
Revenues over (under) expenditures	138,602	13,300	151,902
Other financing sources (uses)			
Transfers to primary government	131,400	-	131,400
Change in fund balance / net assets	7,202	13,300	20,502
Fund balance / net assets, beginning of year	217,267	123,400	340,667
Fund balance / net assets, end of year	\$ 224,469	\$ 136,700	\$ 361,169



**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE AND ON INTERNAL
CONTROL OVER FINANCIAL REPORTING BASED ON AN AUDIT OF
FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE
WITH *GOVERNMENT AUDITING STANDARDS***

August 27, 2004

Honorable Mayor and Members
of the City Council
City of Cheboygan
Cheboygan, Michigan

We have audited the financial statements of the governmental activities, the business-type activities, the discretely presented component unit, each major fund, and the aggregate remaining fund of the ***City of Cheboygan*** (the "City"), as of and for the year ended June 30, 2004, and have issued our report thereon dated August 27, 2004. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the City's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the City's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. However, we noted certain matters involving internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the City's ability to record, process, summarize and report financial data consistent with the assertions of management in the financial statements.

The reportable condition is described as follows:

Due to staff size, there is limited segregation of duties over cash receipts and the recording of these transactions. The City recognizes this risk, but no change will be implemented because the costs would exceed the benefits.

Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses. However, we noted other matters involving the internal control over financial reporting that we have reported to management of the City in a separate letter dated August 27, 2004.

This report is intended solely for the information and use of the audit committee, management, others within the organization, and the City Council and is not intended to be and should not be used by anyone other than these specified parties.





REHMANN ROBSON

Certified Public Accountants

A member of THE REHMANN GROUP

An Independent Member of Baker Tilly International

August 27, 2004

Honorable Mayor and Members
of the City Council
City of Cheboygan
Cheboygan, MI 49721

Through our role in performing financial statement services for the past several years, we have become familiar with your systems, operations and management team. As we work with our clients, we strive to provide direction and constructive feedback to help facilitate their success. The better we get to know you and your objectives, the more we can offer in terms of proactive advice.

In planning and performing our audit of the financial statements of the *City of Cheboygan* for the year ended June 30, 2004, we considered the City's internal control structure to determine our auditing procedures for the purpose of expressing an opinion on the financial statements and not to provide assurance on the internal control structure.

The memorandum that accompanies this letter summarizes comments related to future financial reporting responsibilities and other matters facing the *City of Cheboygan*. This letter does not affect our report dated August 27, 2004 on the financial statements of the *City of Cheboygan*.

We have already discussed these comments with the City Manager and City Clerk-Treasurer, and we would be pleased to discuss them in further detail at your convenience, to perform any additional study of these matters, or to assist you in implementing the recommendations.

Best wishes for a successful 2004-2005.

Encl.1

CITY OF CHEBOYGAN

COMMENTS AND RECOMMENDATIONS

JUNE 30, 2004

Financial Statement Reporting Model

Congratulations! The City successfully completed the challenging task of implementing Governmental Accounting Standards No. 34 reporting model for the fiscal year ended June 30, 2004. Although this was a difficult and time-consuming task for the staff of the City, they worked diligently and should be commended for their commitment to this project.

New Governmental Accounting Standard

The Governmental Accounting Standards Board (GASB) has issued Statement No. 45, *Financial Reporting by Employers for Post-Employment Benefit Plans other than Pension Plans*.

This standard requires the City determine the present value of the projected future cash payments for retirees healthcare benefits. The City will then be required to make annual contributions to fund these costs, similar to the process that the City is currently following for its Municipal Employees Retirement System Plan .

The GASB Statement No. 45 allows governmental units with less than 100 participants to choose to contract with an actuary or prepare their own estimates using a simplified alternative measurement method. This alternative method includes the same broad measurement steps that an actuary would use; however, it permits simplification of certain assumptions to make the method usable by non-specialists.

Although the City is not required to adopt this standard until the fiscal year ending June 30, 2010, early implementation is encouraged. The City should begin to plan for this implementation by determining whether they should contract with an actuary or if City management will be performing the required calculations. Further the City will need to determine whether they will hold these annual contributions in a fund of the city or if they will establish a trust fund which would be administered by a third party.

We would be happy to provide additional information necessary to assist the City in implementing GASB Statement No. 45.

Liability for Accrued Sick and Vacation

As of June 30, 2004, the City's liability for accrued sick and vacation is approximately \$235,000. The City has approximately \$119,000 reserved for related benefits available to employees upon retirement. The City should continue to monitor the cash flow requirements to retire this liability based on the expected retirement date and expected individual payout amounts related to each employee of the City. This will ensure that the City has the appropriate cash flow when its employees retire and will also provide the necessary information for the City to budget the required annual General Fund transfer.

Michigan Finance Qualifying Statement

Beginning January 1, 2004, all governmental units subject to the Revised Municipal Finance Act (PA 34 of 2001) must submit their qualifying statement electronically using the Department of Treasury's website. The City Treasurer-Clerk must call the Local Audit and Finance Division of the Department of Treasury (517) 373-0660 and establish a password in order to submit the qualifying statement electronically. The Qualifying Statement is due to the Michigan Department of Treasury no later than six months after the City's fiscal year end.

Electronically Filing the Financial Statements

The Michigan Department of Treasury (the "Treasury") has issued Numbered Letter 2004-5 which requests (under the authority of Michigan Compiled Law 141.427(1)) that all audits required in accordance with Public Act 2 of 1968 and Public Act 71 of 1919 be submitted electronically to the Treasury in a Portable Document Format (PDF) compatible with Adobe Acrobat. Although this filing process is not mandated at this time, the Treasury is strongly recommending that all governmental units file their year end audit reports including the Auditing Procedures Report (496) and management comment and recommendation letter electronically. We have provided the necessary information, in this electronic format, to the City Treasurer-Clerk to enable the City to comply.

Conclusion

As always, it has been a pleasure to provide audit services to the ***City of Cheboygan***. The City's accounting personnel are very conscientious and most helpful. The accounting records were in good order and all audit information requests were satisfied promptly.

We appreciate your business! Thank you.